RULE 144A, REGULATION S AND AMENDING THE GLASS-STEAGALL ACT: A NEW LOOK AT FOREIGN BANKS AND FOREIGN ISSUERS PARTICIPATING IN THE UNITED STATES SECURITIES MARKET

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INTRODUCTION

There is a trend in the capital markets of the world toward more interaction between once seemingly isolated markets.[1] Increasingly, the walls are coming down in an expeditious fashion and the United States Securities and Exchange Commission (SEC) is taking part in this globalization.[2] Through a prudent step-by-step approach,[3] the SEC, by adopting Rule 144A and Regulation S, has increased the possible sources from which foreign issuers can more easily raise capital while retaining regulatory integrity. In the same step, the SEC has made it easier to introduce domestic investors to potentially lucrative investments in security issuances that originated abroad.[4]

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1. *See* H. BLOOMENTHAL, EMERGING TRENDS IN SECURITIES LAW § 10.04, at 10-17 (1989 ed.) [hereinafter H. BLOOMENTHAL (1989 ed.)]

2. Brady, *Evolution, not Revolution*, EUROMONEY, June 1990, at 47. *See also* H. BLOOMENTHAL, EMERGING TRENDS IN SECURITIES LAWS 7-1 (1990 ed.) [hereinafter H. BLOOMENTHAL (1990 ed.)]

3. For purposes of Rule 144A of the Securities Act of 1933, foreign bank means any entity defined as a foreign bank by Rule 6c-9(b)(2) and (3) of the Investment Company Act of 1940. *See Resale of Restricted Securities; Changes to Method of Determining Holding Period of Restricted Securities Under Rules 144 and 145*, Securities Act Release No. 6862 [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,523 (Apr. 27, 1990) [hereinafter Securities Act Release No. 6862]. Rule 6c-9(b)(2) and (3) define the term foreign bank as "a banking institution incorporated or organized under the laws of a country other than the United States that is: (i) regulated as such by that country's government or any agency thereof; (ii) engaged substantially in commercial banking activity; and (iii) not operated for the purpose of evading the provisions of the Act." "Engaged substantially in commercial banking activity" means engaged regularly in, and deriving a substantial portion of its business from, extending commercial and other types of credit, and accepting demand and other types of deposits, that are customary for commercial banks in the country in which the head office of the banking institution is located.

4. *See id.* The SEC stated that the adoption of Rule 144A should be viewed as an initial step and that the SEC will monitor its success and failures with respect to implementing its purpose and upholding the objectives of United States securities laws. *Id.* In a poll conducted by Business Wire Inc., 50% of the respondents said they would invest in securities offered under Rule 144A within the next two years. *U.S. Investors to Significantly Broaden International Focus*, Business Wire (June 15, 1990) [hereinafter Business Wire]. Trading in foreign securities provides investors with greater flexibility to take advantage of healthier economies,

Rule 144A establishes a new non-exclusive exemption from the registration requirements of the Securities Act of 1933 (Securities Act) and the Securities and Exchange Act of 1934 (Exchange Act) for the resale of privately placed securities by persons other than the issuer to certain qualified institutional buyers (Rule 144A transaction).[5] In conjunction with Regulation S, which establishes the criteria for a permissible offshore unregistered securities offering pursuant to the Securities Act, the SEC has created a new vehicle by which foreign private issuers and qualified foreign banks can participate in securities markets at home and abroad.[6]

One of the SEC's immediate goals in adopting Rule 144A is to facilitate more "liquid and efficient" trading in foreign securities by large institutional investors in the secondary market.[7] The SEC's intent is not necessarily to limit the market created by Rule 144A to large institutional investors and exclude smaller sophisticated investors, but rather to expand the resale market on a trial basis.[8] Regulation S furthers the SEC's goals by reducing prior restrictions on exempt offshore offerings by foreign issuers. As a result, liquidity is promoted in the Rule 144A secondary market.[9] Beyond Rule 144A and Regulation S, the further opening of the United States securities market to foreign private issuers and banks depends on, among other things, the amount of trading activity in foreign securities balanced by the need to protect unsophisticated investors.[10] Amending the Glass-

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minimize exposure to short-term erratic behavior on one nation's stock or bond market and protect assets from temporary weakness of the United States dollar. *See* Note, *International Securities Trading: The United States and Great Britain Develop Clearing and Settlement Procedures for a New Age*, 19 CAL. W. INT'L L.J. 129 (1988).

5. *See* Securities Act Release No. 6862, *supra* note 3. Rule 144A facilitates trading in domestic as well as foreign issued securities. *Id.* However, this Article specifically discusses Rule 144A and Regulation S and amending the Glass-Steagall Act as each affects foreign private issuers and foreign banks. Accordingly, the text of this Article will reflect such focus. Its discussions are equally applicable to domestic issuers and domestic banks.

6. *See Offshore Offers and Sales*, Securities Release No. 6863, (Apr. 24, 1990) [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,524 (Apr. 24, 1990) [hereinafter Securities Act Release No. 6863].

7. *See supra* note 3 and accompanying text.

8. *Id.*

9. *See* H. BLOOMENTHAL (1990 ed.), *supra* note 2, § 7.23 (2)(c), at 7-64. Regulation S may be viewed as enhancing the liquidity of the secondary market created by Rule 144 by permitting securities to be traded outside its closed trading structure. *See id.*

10. *See supra* note 3. For competitive reasons, such as, the growth of the United States securities market vis-a-vis the growth of other foreign markets, and regulatory reasons, the SEC has considered expanding the types of possible offerings in the United States. *See* H. BLOOMENTHAL (1989 ed.), *supra* note 1, § 10.4[4], at 10-17. "These rules will have a profound and beneficial effect on the ability of issuers to raise capital in the context of today's global market place and enhance the competitiveness of our domestic market." Bush, *Interna-*

Steagall Act to permit banks to engage in heretofore prohibited securities activities will facilitate this expansion, and permitting trading by banks in Rule 144A securities may represent a beginning in modifying U.S. banking law.[11]

This Article suggests that many foreign private issuers,[12] and eligible institutions, will be unnecessarily prohibited from participating in this newly created secondary market.[13] Limitations and restrictions built into Rule 144A regarding foreign private issuers may unfairly prevent their access to the secondary market, including access to securities eligible for sale on PORTAL,[14] the newly created automated-quotations system designed to facilitate trading in Rule 144A securities, or its equivalent.[15]

In addition, foreign banks may be unnecessarily prevented from participating in this market. Limitations set forth in the Investment Company Act of 1940 (Investment Act) may prevent foreign banks from issuing securities eligible for resale under Rule 144A.[16] Foreign banks also face arguably unnecessary restrictions in the criteria used to establish a foreign institution's qualification to act as a buyer in a Rule 144A transaction.[17] Furthermore, applicable banking law, read in conjunction with Rule 144A, creates barriers to trading in the secondary market for foreign banks not encountered by other institutions

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tional Capital Market, Fin. Times, July 2, 1990, Part V, at 5 (quoting Mr. Richard Breeden, SEC Chairman) [hereinafter Bush, Fin. Times].

11. Legislation has recently been introduced in Congress to amend the Glass-Steagall Act and permit banks to engage in non-banking activities such as financing new stock issues heretofore prohibited by the Glass-Steagall Act. N.Y. Times, Feb. 21, 1991, at D6, col. 2. The newly empowered non-banking activities would be conducted separately from the traditional lending part of the bank, behind "firewalls." *Id.* Jan. 29, 1991, at A16, col. 1.

12. *See* 17 C.F.R. § 240.3b-4 (1990). A foreign private issuer is an entity incorporated outside of the United States, 50% or more of whose record holders have addresses outside of the United States. If 50% or more of the issuer's record holders have United States addresses, it can maintain foreign private issuer status so long as none of the following apply: (i) a majority of its directors or executive officers are United States citizens or residents, or (ii) more than 50% of its assets are located in the United States, or (iii) its business is administered principally in the United States. *See id.*

13. *See infra* notes 293-304 and accompanying text.

14. *See infra* notes 243-259 and accompanying text. The American Stock Exchange has also proposed an automated quotation system for use in conjunction with Rule 144A transactions called SITUS - "System for Institutional Trading of Unregistered Securities." *See* Quinn, Taylor & Klien, *Internationalization of the Securities Markets*, in Advanced Securities Law Workshop 7, 34 (Practising Law Institute Handbook No. 703 (1990)) [hereinafter Quinn].

15. In June 1990, the American Stock Exchange announced it was developing an automated quotation system called SITUS that would facilitate trading in securities eligible for trading under Rule 144A. This system would compete directly with PORTAL.

16. *See infra* notes 260-280 and accompanying text.

17. *See infra* notes 243-259 and accompanying text.

participating as buyers.[18] Nevertheless, the adoption of Rule 144A and Regulation S come at a time of increased activity in the traditional private placement market; foreign issuers, as well as foreign banks, may wish to take advantage of this new market.[19]

Traditionally, the secondary private placement securities market involves trading in debt instruments in complex transactions.[20] Typically, large institutions, in particular large insurance companies, purchase debt instruments in reliance on the private placement exemption of the Securities Act.[21] These institutions purchase such instruments for balance sheet rather than investment purposes in closely negotiated transactions.[22] Generally, these are high yield debt instruments, held long term and matched with a corporation's liabilities.[23] As a result, the issuer pays a premium to the institutional buyer to acquire them.[24] Profit for the institutional buyer in this market is acquired by the instrument's high yield and premium.[25] The private placement market in such debt instruments has been characterized as essentially illiquid; there is no active subsequent trading in the debt instruments.[26]

The market as shaped by Rule 144A and Regulation S, may revolutionize the secondary market and move the private placement market toward trading in privately placed equity securities for investment

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18. *See infra* notes 378-392 and accompanying text.

19. *See* Bush, Fin. Times, *supra* note 10, at 5.; *See also* Business Wire, *supra* note 4. Respondents to a poll conducted by the Business Wire stated they expected to increase their participation in offerings by foreign companies as a result of Rule 144A. *Id.* *See* H. BLOOMENTHAL (1989 ed.) *supra* note 1, at § 8.09. The private placement market has grown steadily over the past decade. Bush, Fin. Times, *supra* note 10, at 5. In 1980 the market had $15.8 billion in new issues compared to $170 billion in 1989 and it is expected to reach $250 billion by the end of 1990. *Id.*

20. The secondary market created by Rule 144A is new in that it defines the legal parameters in which an institution may resell securities within a safe-harbor. The market, however, has existed under the § 4(1-1/2) exemption essentially for trading in debt instruments involving complex transactions. Dash, *The Private Placement Alternative: Advantages and Disadvantages*, in PRIVATE PLACEMENTS 1990: CURRENT DEVELOPMENTS IN PRIVATE FINANCING 535-37 [hereinafter Dash, *Private Placement Alternative*]; Panel discussion, Practising Law Institute Seminar, New York City (July 24, 1990) [hereinafter Panel Discussion]; *SEC Rule 144A: A New Market*, Fin. Reg. Rep (May 1990) [hereinafter *SEC Rule 144A: A New Market*].

21. *Managers Eyeball Strategies in Wake of 144A*, BONDWEEK, May 7, 1990, at 1.

22. *See* Dash, *Private Placement Alternative*, *supra* note 20, at 535-37.

23. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 6-2.

24. *See* Dash, *Private Placement Alternative*, *supra* note 20, at 535-37.

25. *Id.*; *See* Longa, *U.S. Corporate Finance*, Reuters, July 2, 1990 [hereinafter *U.S. Corporate Finance*].

26. *See* Dash, *Private Placement Alternative*, *supra* note 20, at 535-37.

purposes.[27] It is hoped that trading in this market will occur often and holding periods will be short.[28] An institution's profit will be realized by capturing the raise in the security's value in a liquid market.[29]

Foreign issuers should be attracted to this domestic secondary market. The new Rule 144A exemption allows foreign equity securities[30] to be freely traded among investors operating in the United States securities market without being subject to the onerous and often costly disclosure requirements associated with registration under the Securities Act and the Exchange Act.[31] Lack of privacy, as a result of corporate information being disclosed, is of particular concern to foreign investors.[32] Consequently, throughout this Article, the disclosure requirements of the principal United States security laws will be reviewed and compared with applicable disclosure requirements of the security laws of foreign jurisdictions.

Furthermore, Regulation S permits a foreign issuer or a qualified buyer to resell Rule 144A securities in the offshore market and, in tandem with Rule 144A, enables the creation of new and imaginative ways to raise capital.[33] Accordingly, foreign issuers will have to structure and market their offerings in consideration of the legal requirements established by Rule 144A, Regulation S and related applicable securities laws.[34]

On the other hand, foreign banks, should they overcome certain obstacles and/or should applicable securities laws and banking laws be amended to remove such obstacles, have an opportunity to compete in the secondary market as buyers. Foreign banks can further diversify their business activities, act as equity holders and raise capital through risk-management in securities trading, rather than by traditional lending.[35] In addition, foreign banks may be able to expand participation as foreign issuers and raise capital by stock issu-

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27. *See infra* notes 253-257 and accompanying text.

28. *See id.*

29. *See id.*

30. *See id.*

31. *See* Rule 144A, 55 Fed. Reg. 17,945 (Apr. 30, 1990) (codified at 17 C.F.R. § 230.144A) [hereinafter Rule 144A]; Reuters, FIN. REPORT, July 2, 1990. Deregulation of the market by Rule 144A has made the United States capital markets more attractive to more issuers. *Id.* Foreign issuers are also concerned about potential and significant liability under United States securities law.

32. *See* Bush, Fin. Times, *supra* note 10, at 5. Large institutions generally prefer a private offering because it is less expensive, less regulated and avoids registration. *Id.*

33. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at § 7.01(1).

34. *See infra* notes 394-420 and accompanying text.

35. *See infra* notes 260-277 and accompanying text.

ances alongside traditional lending methods.[36] To participate competitively and effectively as buyers in this market, foreign banks will need to position themselves in this market with international brokerage houses, United States banks and other affiliates, and structure their purchases or issuances of restricted securities with respect to the modified holding periods established under Rule 144.[37]

Part I of this Article will examine the historical access by foreign private issuers to domestic investors with respect to their issuances of equity stock. One method that foreign issuers have used to place their securities with United States investors is through one of the private placement exemptions of the Securities Act.[38] As discussed later, Rule 144A requires a private placement by the issuer prior to commencing trading on PORTAL.[39] Consequently, qualifying under a private placement exemption will continue to be an important step in selling foreign issued securities in the United States.[40]

Part II, Part III and Part IV of this Article will review Rule 144A, Regulation S and PORTAL, and examine their application to foreign issuers, foreign banks and the possible expansion of secondary market trading in foreign equity securities. Certain restrictions set forth in Rule 144A inhibit the creation of an effective secondary market trading in equity securities which may unnecessarily prohibit foreign issuers from participating in this new market.

Part V will examine the sale of foreign banks' securities in this newly created secondary market and discuss the effect applicable United States banking laws may have on foreign banks' participation in Rule 144A transactions. As set forth in Part V, subpart B, the creation of an effective resale market in equity securities under Rule 144A with foreign banks participating as buyers will be limited by other applicable statutory and regulatory securities trading prohibitions. Part VI will discuss changes that might be made to the securities and banking laws to permit wider participation by foreign banks in Rule 144A transactions. Part VII analyzes the structure foreign issuances should take under Rule 144A and Regulation S, including,

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36. *See infra* notes 260-277 and accompanying text.

37. *See infra* notes 120-123 and accompanying text; AM. BANKER, May 4, 1990, at 4.

38. Zaitzeff, *Foreign Bank Participation in the United States Capital Markets*, 2 TOURO L. REV. 19, 45 (1985) [hereinafter Zaitzeff]. Traditionally, the exemption from registration under the Securities Act pursuant to § 4(2) and Regulation D of the Securities Act have been referred to as the private placement exemptions. *Id.*

39. *See* Rule 144A, *supra* note 31.

40. *Id.*

disclosure requirements, contractual covenants and other filing requirements under the Securities Act and Exchange Act.

I. Historical Perspective: The Placement of Foreign Securities in the United States Securities Market

Historically, the SEC has sought to control the trading of foreign securities in United States markets much the same as it controls domestic securities.[41] Under section 5 of the Securities Act, a foreign issuer must register its securities with the SEC if it makes use of any means of interstate commerce or the United States mails to offer or sell its securities.[42] Under section 12 of the Exchange Act, an issuer may be subject to registration, reporting and disclosure requirements if its shares are traded publicly.[43] Foreign issuers generally find these domestic securities law requirements too expensive, and view the required disclosure as overly intrusive into their affairs.[44]

In contrast, regulation of a foreign issuer's securities by the laws and rules applicable in its home country are often not as rigorous as United States law.[45] Because foreign governments choose not to regulate their securities markets as stringently as the SEC, the costs associated with raising capital abroad may be lower and the disclosure is less intrusive than that required by the SEC.[46] Consequently, foreign issuers may prefer not to offer their securities publicly in the United States, or to nationals living abroad. Foreign issuers seek some means to sell their securities in the United States without registering under the Securities Act or Exchange Act.[47]

A principal alternative for a foreign issuer, other than a public offering to United States investors, is to utilize a private placement exemption.[48] Generally, a private placement is a transaction which the SEC deems not a public offering; thus, the filing of a registration statement is not required.[49] As a result of the transaction's exempt

41. H. Bloomenthal, International Capital Markets and Securities Regulation § 5.07[1], at 5-53, 5-60 (1990) [hereinafter H. Bloomenthal, International Capital Markets].

42. 15 U.S.C. § 77(e) (1988).

43. *Id.* at § 771.

44. *See* H. Bloomenthal (1990 ed.), *supra* note 2, at § 5.03(3)(d), 5-23.

45. *Id.* at § 7.03(2)(B), at 7-11; Miller, *New U.S. Securities Rule Threatens Euromarkets, Bankers Say*, Reuter Library Report, June 1, 1990.

46. H. Bloomenthal (1989 ed.), *supra* note 1, at §§ 10.02(1), 10-11, 10.04(1), 10-17.

47. *See* Bush, Fin. Times, *supra* note 10.

48. Zaitzeff, *supra*, note 38, at 45.

49. *See* 15 U.S.C. § 77d(2) (1988); 17 C.F.R. § 230.501-203.506 (1990).

status, a private placement's registration costs and disclosure requirements are generally not as prohibitive as those of a public issuance.[50]

Since 1980, the bulk of foreign securities placed in the United States have occurred through private placements.[51] A traditional method employed by foreign private issuers to place their securities in the United States market has been by means of section 4(2) of the Securities Act and Rule 506 of Regulation D, adopted pursuant to the Securities Act.[52] These two exemptions are often referred to as the "private placement" exemptions.[53] As mentioned above, in order to participate in a Rule 144A transaction the issuer's securities must originally be placed pursuant to either of these two private placement exemptions.[54]

A. Section 4(2): The Private Placement Exemption

Section 4(2) of the Securities Act has been a principal method of exempting securities from the registration requirements of the Securities Act.[55] Section 4(2) exempts "transactions by an issuer not involving any public offering." The exemption is generally available to any foreign private issuer offering its securities to institutional investors, or a limited number of private investors, who can be characterized as "sophisticated."[56] Unlike other exemptions, the section 4(2) exemption is broadly drafted and its applicability to a particular transaction is dependent on judicial and administrative interpretation.[57] The exemption applies to transactions and not securities. Thus, a foreign private issuer that fails to meet the explicit criteria of another statutory exemption could rely on the section 4(2) exemption.[58]

As discussed in more detail below, Rule 506 clarifies the criteria the SEC employs to evaluate whether an offering qualifies as a private placement for section 4(2) purposes.[59] The criteria set forth in Rule

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50. *See* Bush, Fin. Times, *supra* note 10, at 5.

51. *See supra* note 19 and accompanying text.

52. *See* Zaitzeff, *supra* note 38, at 45.

53. *Id.*

54. Rule 144A, *supra* note 31.

55. *See supra* note 20 and accompanying text.

56. 15 U.S.C. § 77d; *See also* SEC v. Ralston Purina Co., 346 U.S. 119 (1953). No precise definition of "sophistication" exists. Generally, an entity is deemed sophisticated if it can "fend for itself" without protection of the United States securities laws. The definition of purchaser under Rule 506 of Regulation D has been suggested to be a definition of sophistication. *See infra* note 85.

57. *See* Zaitzeff, *supra* note 38, at 45.

58. *Id.* For example, an offering which failed to qualify under Rule 506 could nonetheless be considered exempt under § 4(2).

59. 17 C.F.R. § 230.506(a) (1990). Rule 506 provides that a securities offering under-

506 operates only as a guideline, and non-compliance with Rule 506 does not create an inference that the transaction will not be exempt under section 4(2).[60] Also, Rule 506 functions as a separate safe-harbor.[61] Notwithstanding the criteria set forth in Rule 506, the Supreme Court of the United States in *SEC v. Ralston Purina Co.* established the following four principal factors that are generally determinative as to the availability of the section 4(2) exemption: (i) the nature and number of offerees, (ii) the type of information disclosed to the offerees, (iii) the offerees' access to information, and (iv) the size of the offering.[62]

In *Ralston Purina*, the Court ruled that in order to qualify for a section 4(2) exemption, all offerees should be sufficiently sophisticated to comprehend the information provided them.[63] Although the Court did not stress a specific number of offerees as a significant factor, the implicit holding is that the fewer the number of offerees the better.[64] The second factor outlined above is generally viewed as requiring a relationship between the offeree and the issuer sufficient to enable the offeree to obtain adequate information from the issuer so an informed investment decision can be made.[65] Furthermore, *Ralston Purina* and subsequent judicial and administrative interpretations established that, in consideration of the third factor, the issuer should be in a position to provide an offeree with the same disclosures required in an offering under the Securities Act.[66] Complying with the exemption may seem intrusive, but given the small number of purchasers typically involved and the close relatonship usually existing between the parties, such a requirement is not considered burdensome.[67] Finally, the size of the offering in terms of the participants and number of shares, though less determinative in establishing whether an exemption exists, is significant in terms of controlling downstream sales.[68] The greater the number of participants and shares sold, the more

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taken pursuant to the rule shall not be considered an "offering within the meaning of section 4(2) of the [Securities] Act." *Id.*

60. Zaitzeff, *supra* note 38, at 45.

61. *See* 17 C.F.R. § 230.506 (1990).

62. *See Ralston Purina Co.*, 346 U.S. at 119.

63. *See id.* at 125.

64. *See id.*

65. *See* Zaitzeff, *supra* note 38, at 47; SEC v. Continental Tobacco Co., 463 F.2d 137 (5th Cir. 1972).

66. *See* Securities Act Release No. 45,227 Fed. Reg. 11,316 (1962), *reprinted in* 1 Fed. Sec. L. Rep. (CCH) ¶ 2770, at 2918 (Nov. 6, 1962). *Ralston Purina*, 346 U.S. at 127.

67. *See supra* notes 20-26 and accompanying text.

68. *Ralston Purina*, 364 U.S. at 125; Zaitzeff, *supra* note 38, at 48.

likely the securities will reach the general investing public.[69] Consequently, the greater the number of participants and shares sold the less likely the SEC will find an offering is exempt, notwithstanding the inclusion of strict resale provisions in the private placement agreements.[70]

As a result of restrictive case law interpretations, SEC rulings and the nature of the participants in a section 4(2) offering, foreign issuers and United States investors use the exemption chiefly for the issuance of long term, high-yield debt instruments.[71] Furthermore, debt instruments receive the most benefits from the market created by section 4(2). This is true because, in large measure, no effective resale exemption exists, other than Rule 144 and the section 4(1-1/2) resale exemption (the bar created exemption to facilitate the resale of privately placed debt and other instruments),[72] both of which subject owners of securities to lengthy holding periods prior to the securities being eligible for public resale.[73] Consequently, once securities are purchased in a private placement they may not be resold for some time without jeopardizing the exempt status of the issuer's offering.[74]

Nevertheless, as discussed in Part II, Rule 144A permits the immediate resale and trading on PORTAL of privately placed securities.[75] As a result, Rule 144A may function best as an exemption for the resale of equity securities just as section 4(1-1/2) functions as an

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69. Zaitzeff, *supra* note 38, at 38.

70. *Id.*

71. *See supra* notes 20-26 and accompanying text.

72. J.W. HICKS, RESALE OF RESTRICTED SECURITIES 486 (1989) [hereinafter J.W. HICKS]. A § 4(1-1/2) exemption is a "hybrid exemption not specifically provided for in the [Securities Act] but clearly within its intended purpose." *Id.* (citing Securities Act Release No. 6188 (Feb. 1, 1980)). The § 4(1-1/2) exemption is based primarily on § 4(1) of the Securities Act which exempts certain transactions by persons who are not issuers, dealers or underwriters. 15 U.S.C. § 77(d)(1) (1988). However, the SEC has stated that it contemplates private sales effected in a similar manner as a private placement under § 4(2). J.W. HICKS, *supra* note 72, at 469. Accordingly, many of the criteria to evaluate the manner of the offering under §§ 4(1) and 4(2) will be used to determine the existence of a § 4(1-1/2) exemption. *Id.*

73. Rule 144 requires a person to hold a security instrument anywhere from two to three years. 17 C.F.R. § 230.144 (d)(K) (1990). The § 4(1-1/2) exemption likewise contemplates a sufficiently long holding period to assure that the buyer of the security is assuming the economic risk of his purchase. J.W. HICKS, *supra* note 72, at 504. The value of an equity security is often shaped by market forces and active trading. A holder of an equity security generally profits by its increase in value. A prolonged holding period removes such activity. In contrast, a debt instrument is typically valued against the assets of the issuer.

74. *See* J.W. HICKS, *supra* note 72, at 91. Only a limited number of resale exemptions exist pursuant to which a person may sell its restricted private placement securities. *Id.* Generally, a public sale by any other means is prohibited unless registered under the Securities Act. 15 U.S.C. § 77(d) (1988).

75. Rule 144A, *supra* note 31.

exemption for the resale of debt instruments.[76] Indeed, the limitations that have traditionally shaped a section 4(2) private placement may no longer exist and the economic feasibility of a foreign private issuer offering its equity securities in the United States may be enhanced.[77]

A foreign issuer, therefore, will have to structure its private placement appropriately to enable its securities to be traded on PORTAL. As discussed in Part II, a foreign issuer only participates in a Rule 144A transaction indirectly, but its profit may be directly dependent on this indirect participation. For example, in structuring a section 4(2) exemption, a foreign private issuer should, among other things, avoid public advertising of its offering in the United States to prevent the loss of its initial private placement status. Also, the private foreign issuer should require that the offeree agree in writing not to resell the securities unless this is done in accordance with Rule 144A or some other legally available means of resale.[78] More importantly, as discussed in Part II, a foreign issuer anticipating a subsequent distribution of its equity securities through PORTAL should be aware that certain types of equity stock may be ineligible for trading on PORTAL.[79] Nevertheless, a private offering that is undertaken with the express intent to resell the securities under Rule 144A will not affect the exempt status of the offering under section 4(2) or Rule 506.[80]

B. Rule 506 of Regulation D: The Safe-Harbor for Private Placements

A private securities offering under the Rule 506 exemption, like the exemption provided under section 4(2) of the Securities Act, must meet a series of quantitative and qualitative criteria to establish the availability of the exemption.[81] Unlike section 4(2), however, Rule 506 imposes strict limitations on the number and nature of purchas-

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76. *See* Hanks, *Securities Law Update*, N.Y.L.J., May 10, 1990, at 5. Prior to Rule 144A, the § 4(1-1/2) exemption was the principal method of effecting a private resale of securities. *Id.*

77. *Id.* The traditional private placement market will no longer exist in the same sense that an active resale market exists for certain privately placed securities on an automated quotation system. Equity securities may derive a substantial portion of their perceived value by active trading on this market. The market will assess the issuers worth as reflected in the price of its share. *See* Garten, *Regulatory Growing Pains: A Perspective on Bank Regulation in a Deregulatory Age*, 57 FORDHAM L. REV. 501, 546 (1989) [hereinafter Garten].

78. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 5-22.

79. *See infra* notes 161-169 and accompanying text.

80. *See infra* note 92.

81. *See supra* notes 58-60.

ers. If such conditions are not met, the transaction is not exempt.[82] Under Rule 506, an exemption from the registration requirements of section 5 of the Securities Act may be available to a foreign private issuer who limits the offering of securities to thirty-five purchasers or less.[83]

In calculating the number of purchasers, the Rule expressly excludes "accredited investors" from inclusion in the number of purchasers.[84] These investors, such as banks or natural persons whose net worth exceeds $1,000,000 are deemed sufficiently sophisticated to judge their investment risk. Under Rule 506, an issuer may offer its securities to any number of accredited investors.[85] Rule 506, however, sets out a separate test for purchasers. To qualify as a purchaser, a person must have knowledge and experience in financial matters and be capable of evaluating the investment risk.[86]

Any person found to be a purchaser rather than an accredited investor must be furnished investment information regarding the foreign private issuer by the issuer prior to sale.[87] The nature of the disclosure and the amount of information provided is directly dependent on the value of the offering.[88] For example, an issuer not subject to the reporting requirements of sections 13 or 15(d) of the Exchange

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82. 17 C.F.R. § 230.506 (1990).

83. *Id.*

84. *Id.* at § 203.506(b)(2)(ii); *See also id.* at § 501(e).

85. 17 C.F.R. § 230.501(a) (1990). Generally, an accredited investor is any person who falls "within any of the following categories, or who the issuer reasonably believes comes within" such categories:

(1) Any bank, savings and loan institution, broker dealer, insurance company, investment company as defined under the Securities Act or a small business investment company as defined under the Small Business Investment Act of 1958, or any State employee benefits plan with total assets exceeding $5,000 and other certain employee benefit plans;
(2) Any private business development company as defined in the Investment Advisers Act of 1940;
(3) Any organization described in § 501(c)(3) of the Internal Revenue Code, corporation, Massachusetts or similar trust, or partnership with assets exceeding $5,000,000;
(4) Any director, executive officer, or general partner of the issuer, or any director, executive officer, or general partner of a general partner of the issuer;
(5) Any natural person whose net worth at the time of purchase exceeds $1,000,000;
(6) Any natural person who had individual income in excess of $200,000 in each of the two most recent years and has a reasonable expectation of attaining that level of income in the current year; and
(7) Any entity in which the equity owners are accredited investors.

Id.

86. *Id.* at § 230.506(b)(ii).

87. *Id.* at § 230.502(b)(1).

88. 17 C.F.R. § 230.502(b)(2).

Act[89] whose offering exceeds $7,500,000 must provide the same information required in Part I of the registration statement that is normally needed for use in a public offering, and audited financial statements must be provided within 120 days of the offering.[90] A foreign issuer may be required to disclose the information required in Form 20-F.[91] Accordingly, the amount of information provided by an issuer offering securities of significant value may be equivalent to the information provided in a public offering. A less significant offering by a reporting issuer would require less disclosure to the purchaser.[92]

A foreign issuer must also comply with broad limitations on the nature of the offering, including: (i) a prohibition on the use of certain means of advertising and solicitation to offer or sell its securities and (ii) a strict prohibition on the unregistered non-exempt public resale of its securities. This second element may require a reasonable inquiry by the issuer into the purchaser's motive for buying the securities, written disclosure to the purchaser that the securities are restricted securities and the placing of a restrictive legend on the cer-

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89. Section 13 of the Exchange Act requires every issuer, domestic and foreign, that has securities registered pursuant to § 12 of the Exchange Act to file periodic and other intermittent reports with the SEC and any national securities exchange which lists the issuer's securities. 15 U.S.C. § 78(m) (1988). A foreign issuer eligible to use Form 20-F (the annual report and registration statement for foreign private issuers) may satisfy the reporting requirements under § 13 by filing Form 20-F within six months after the end of its fiscal year and providing the SEC interim reports on Form 6-K. *Id.* Under § 15(d) of the Exchange Act, a foreign private issuer that has registered its securities under the Securities Act is required to provide the same information and reports required under § 13 of the Exchange Act. *Id.* at § 780(d). These reporting requirements are suspended, however, if the class of registered shares of the issuer is held by fewer than 300 persons at the beginning of a year or the issuer registers the shares under § 12 of the Exchange Act and files reports under § 13 of the Exchange Act. *Id.*

90. *See supra* note 87. For example, Part I of Form S-1 requires an issuer to disclose: (i) information on the use of the proceeds from the offering; (ii) the offering price; (iii) the plan of distribution; (iv) a description of the offered securities; (v) the interests of named experts and counsel; and (vi) extensive information on the issuer's company, property, legal proceedings and financial situation.

91. *See* Exchange Act Form 20-F. Form 20-F in general requires an issuer to describe: (i) its property holdings; (ii) its legal proceedings; (iii) its direct and indirect ownership; (iv) the trading market or its securities; (v) the taxation of its security holders; (vi) certain financial data covering the past five years; (vii) financial condition and results of operations (MDA disclosure); (viii) directors and officers and their compensation; and (ix) certain related transactions. Foreign issuers often have difficulty meeting these requirements. Their methods of auditing financial data usually differ from generally accepted accounting principles employed in the United States. Reconciling the different reporting requirements is often too expensive.

92. 17 C.F.R. § 230.502(b)(2) (1990). For example, an offering of less than $7,500,000 by a non-reporting issuer would need only the information required by P I of Form S-18 (the short form registration statement) and only financial statements for the most recent fiscal year. *Id.* at § 230.502(b)(2)(B).

tificate evidencing the securities restrictive nature.[93] In addition, rules of integration apply, though an offer made outside the United States in compliance with Regulation S will not be deemed part of the Regulation D offering.[94]

A foreign issuer's privately placed securities may be resold in the United States pursuant to Rule 144A.[95] Consequently, the private placement's statutory resale prohibition must be complied with in sales to qualified institutional buyers.[96] Compliance may be documented through modified forms currently used to restrict resales of securities.[97]

C. Rule 144

Rule 144 is not a private placement exemption.[98] Its role in regulating securities trading occurs after a private placement.[99] Rule 144 regulates the resale of restricted securities to the public that have been held privately for at least two years.[100] Generally, a restricted security is any security that has not been acquired in a public offering (i.e., a private placement).[101] In contrast, Rule 144A regulates the resale of restricted securities to qualified institutional buyers and no holding period is required.[102]

Rule 144 provides a safe-harbor from the registration require-

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93. *Id.* at § 230.502(c) and (d).

94. *Id.* at § 230.502(a).

95. *See infra* notes 129-135 and accompanying text.

96. *Id.*

97. *See infra* notes 440-448 and accompanying text.

98. 17 C.F.R. § 230.144

99. *Id.*

100. *Id.*; *See* Fogelson, *Rule 144-A Summary Review*, 37 BUS. LAW 1519, 1540 (1982). Rule 144 was adopted to provide guidance to the holder of restricted securities wishing to sell them without the need of registration with the SEC. *Id.* Prior to Rule 144, such holder could sell his restricted securities in reliance on the § 4(1-1/2) exemption. Hanks, *Securities Law Update*, N.Y.L.J. May 10, 1990, at 5.

In addition, through the § 4(1) exemption of the Securities Act, a seller may effect a private resale of the issuer's securities. Section 4(1) exempts "transactions by any person other than an issuer, underwriter or dealer" from the Securities Act's registration requirements. 15 U.S.C. § 77(d)(i). Generally, an underwriter is any person who buys securities with the view towards distribution of that security. *Id.* at § 77(b)(ii). This broad characterization made it difficult and potentially hazardous (subjecting the seller to an SEC enforcement action or a civil suit for damages) for a seller to know whether or not it was in compliance with § 4(1). To resolve this uncertainty, Rule 144 was adopted to provide a safe-harbor for sale of restricted securities. *See* 17 C.F.R. § 230.144 (1990).

101. *See id.* Restricted securities are those acquired directly or indirectly from the issuer in a non-public offering. *See id.* at § 230.144(a)(3).

102. *See* Rule 144A, *supra* note 31.

ments of the Securities Act.[103] The Rule was amended to specifically include Rule 144A securities within the definition of restricted securities.[104] Accordingly, a qualified institutional buyer eventually will be able to distribute its Rule 144A securities to the investing public in the United States in reliance on Rule 144.[105] To use the safe-harbor created by Rule 144, however, any holder of restricted securities, including a qualified institutional buyer, will have to comply with certain conditions set forth in the Rule.[106]

Since its inception, Rule 144 traditionally has been the exclusive means by which an affiliate of a foreign issuer may effect a resale of the issuer's restricted shares.[107] The safe-harbor provided by Rule 144 applies to non-affiliates of the issuer as well.[108] This distinction between affiliate and non-affiliate status is important. The preconditions, including the holding period conditions, that must be met to insure that a seller may rely on the safe-harbor created by Rule 144 is determined by whether the holder is an affiliate or a non-affiliate of the foreign issuer.[109]

Under Rule 144, an affiliate of the issuer must satisfy the following conditions prior to effecting a resale of the issuer's restricted securities:

1. Current "public information" on the issuer must be available;[110]

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103. *See* 17 C.F.R. § 230.144 (1990).

104. *See id.*

105. *See id.*

106. Rule 144(b) states:

> Any affiliate or other person who sells restricted securities of an issuer for his own account, or any person who sells restricted or any other securities for the account of an affiliate of the issuer of such securities, shall be deemed not to be engaged in a distribution of such securities and therefore not to be an underwriter thereof within the meaning of § 2(11) of the Act if all of the conditions of this rule are met. 17 C.F.R. § 230.144(b) (1990).

107. *Id.* at § 230.144. Rule 144 defines an "affiliate . . . [as] a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, such issuer." *Id.* at § 230.144(a)(1).

108. *Id.* at § 230.144(k).

109. 17 C.F.R. §§ 230.144 (b) and (k) (1990).

110. Generally, under Rule 144, current public information shall be deemed available only if either of these conditions are met:

> (1) The issuer has securities registered pursuant to § 12 of the Securities Exchange Act of 1934, has been subject to the reporting requirements of § 13 of that Act for a period of at least 90 days immediately preceding the sale of the securities and has filed all the reports required . . . to be filed thereunder during the 12 months preceding such sale; or has securities registered pursuant to the Securities Act of 1933 and has been subject to the reporting requirements of § 15(d) of the Exchange Act for a period of at least 90 days immediately preceding the sale of the securities and has filed all the reports required to be filed thereunder during the 12 months preceding

2. Certain "holding periods" for the restricted security must have elapsed;[111]
3. A limitation on the amount of securities sold may not be exceeded;[112]
4. The manner of sale must be undertaken as required by the Rule;[113] and
5. Under certain circumstances, a notice of the proposed sale must

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such sale. . . . The person for whose account the securities are to be sold shall be entitled to rely upon a statement in the most recent report, quarterly or annually, required and filed by the issuer . . . unless he knows or has reason to believe that the issuer has not complied with such requirements.

Id. at C.F.R. § 230.144(c)(1). *See supra* notes 87-89 for a discussion of §§ 13 and 15 of the Exchange Act.

(2) If the issuer is not subject to §§ 13 or 15(d) of the Exchange Act of 1934 there is publicly available the information concerning the issuer specified in clauses (1) to (14), inclusive, and clause 16 of Rule 15c2-11 under that Act or, if the issuer is an insurance company, the information specified in § 12(g)(2)(G)(i) of the Exchange Act.

Id. at § 230.144 (c)(2).

111. 17 C.F.R. § 230.144(d) (1990). Generally, a minimum of two years must elapse between the later of the date of the acquisition of the securities from the issuer or from an affiliate of the issuer. Additionally, any resale of such securities in reliance on this rule for the account of either the acquiror or any subsequent holder of those securities, and if the acquiror takes the securities by purchase, the two-year period shall not begin until the full purchase price or other consideration is paid or given by the person acquiring the securities from the issuer. *Id.* To determine the holding period, Rule 144 sets out special provisions in the event of: (i) stock dividends, splits and recapitalization; (ii) conversions; (iii) contingent issuance of securities; (iv) pledged securities; (v) gifts of securities; (vi) trusts; and (vii) estates. *Id.* at C.F.R. § 230.144(d)(4). With respect to non-affiliates of the issuer, the holding period is three years. *Id.* at § 230.144(k). Rule 144, as amended, now permits an expanded scope for tacking of the time the securities have been held by others to determine the holding period. 17 C.F.R. § 230.144(k) (1990).

112. 17 C.F.R. § 230.144(e)(1) (1990). The amount of securities sold in reliance upon this rule is limited. Sales by affiliates:

shall not exceed the greater of (i) one percent of the shares or other units of the class outstanding as shown by the most recent report or statement published by the issuer, or (ii) the average weekly reported volume of trading in such securities on all national securities exchanges and/or reported through weeks preceding the filing Form 144, or is no such notice is required, the date of receipt of the order to execute the transaction by the broker or the date of execution of the transaction directly with a market maker.

Sales by persons other than affiliates shall not exceed the amount specified in the above paragraph whichever is applicable, unless the securities have been held longer than three years. *Id.* at § 230.144(c)(2).

113. 17 C.F.R. § 230.144(f) (1990).

Securities must be sold in a "broker's transaction" within the meaning of § 5(5) of the "market maker," as that term is defined in § 3(a)(28) of the Exchange Act, and the person selling the securities shall not: (1) solicit or arrange for the solicitation of orders to buy the securities in anticipation of or in connection with such transactions, or (2) make any payment in connection with the offer or sale of the securities to any person other than the broker who executes the order to sell the securities.

Id.

be filed with the SEC and the seller must have a bona fide intention to sell.[114]

A non-affiliated seller wishing to transact a public sale of an issuer's restricted securities might not be subject to the above requirements, with the exception of the second.[115]

The most significant condition of a subsequent resale of a private foreign issuer's securities by the current holder is the holding period requirement.[116] This requirement prevents the use of Rule 144 to affect resales to the public until the securities have been held for the prescribed holding period by its current holder.[117] An affiliate of the issuer may not resell the restricted securities until the shares have been held for two years.[118] A non-affiliate of the issuer may not unconditionally resell the restricted securities until three years have elapsed since the acquisition of the shares.[119] These holding conditions are intended to regulate and control downstream sales of restricted securities so that the public investor will be sufficiently protected should these securities reach the public market.[120]

Ascertaining whether a privately placed security has been held for a period of time which equals or exceeds the particular holding period is not determined simply by calculating the actual time the securities are in the possession of the present holder.[121] Under Rule 144, a holder is permitted to "tack-on" the time the securities were held by others to determine its holding period.[122] For example, a qualified institutional buyer, under the amended Rule 144, may be able to tack on the time a foreign private issuer's securities were held

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114. 17 C.F.R. § 230.144(h) (1990). If the amount of securities to be sold during any period of three months exceeds 500 shares, or other units, or has an aggregate sales price in excess of $10,000, three copies of a notice Form 144 shall be filed with the SEC; and if such securities are admitted to trading on any national securities exchange, one copy of such notice shall also be transmitted to the principal exchange on which such securities are so admitted. *Id.* The person filing the notice must have a bona fide intention to sell the securities within a reasonable time after the filing of such notice. *Id.* at § 230.144(i).

115. 17 C.F.R. § 230.144(k) (1990).

116. *See* J.W. HICKS, *supra* note 72, at 305. The purpose of the registration requirements of the Securities Act is to provide public investors with information to enable them to make an informed investment decision. *Id.* Unregistered exempt offerings are designed to safeguard public investors. Rule 144 effectively safeguards the public investor through the holding period so that the initial purchaser bears the investment risk associated with the security and prevents rapid subsequent distribution. *Id.* at 204-07.

117. *Id.*

118. 17 C.F.R. § 230.144(d)(1) (1990).

119. *Id.* at § 230.144(k).

120. *See* J.W. HICKS, *supra* note 72, at 206.

121. *See* 17 C.F.R. § 230.144(d) (1990).

122. *Id.*; *See* J.W. HICKS, *supra* note 72, at 207.

by the buyer who acquired the shares pursuant to a private placement (i.e., an accredited investor), provided such buyer is not an affiliate of the foreign private issuer. As another example, if the current holder was the recipient of stock created through a recent stock split, the holding period for the current holder would be deemed to relate back to the acquisition of stock from which the split stock was acquired.[123] The amount of time shares actually are held by a particular person to satisfy the holding period requirement may be less than the required period as long as the time elapsed in the aggregate meets the requirements.

Foreign issuers should be mindful that the amended holding period requirements enable their securities to trickle-down to the public more quickly. Investor confidence in the strength of their securities may be determined in these early stages.[124]

A second significant condition a current holder of restricted stock may have to meet under Rule 144 is providing for the availability of current information regarding the foreign issuer.[125] An example of this would be a non-affiliated qualified institutional buyer that reoffers a restricted stock within three years of, but at a minimum of two years after their issuance. Such institutional buyer would be required to insure the availability of the following information regarding a non-reporting foreign private issuer:

(1) The exact name of the issuer and its predecessor (if any);
(2) The address of the issuer's principal executive offices;
(3) The state of incorporation or jurisdiction of origin of the issuer;
(4) The exact title and class of the issuer's security;
(5) The par or stated value of the security;
(6) The number of shares or total amount of the securities outstanding as of the end of the issuer's most recent fiscal year;
(7) The name and address of the transfer agent;
(8) The nature of the issuer's business;
(9) The nature of products or services offered;
(10) The nature and extent of the issuer's facilities;

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123. *See* 17 C.F.R. § 230.144(d)(4)(A) (1990).

124. *Id.* Because a qualified institutional buyer may tack on the time of the purchaser of the privately placed security, such buyer will not have to wait the full three years prior to offering them pursuant to Rule 144. In addition, foreign issuers are using Rule 144A as a "stepping-stone into the United States capital markets." Bush, *Issuers Greet Rule 144A with Two Cheers*, Fin. Times, June 6, 1990, at 37 [hereinafter Bush, *Two Cheers*]. Certain issuers wish to gain "name recognition" with domestic investors under 144A prior to listing on an American exchange. *Id.*

125. 17 C.F.R. § 230.144(c) (1990).

(11) The name of the chief executive officer and members of the board of directors;
(12) The issuer's most recent balance sheet and profit and loss and retained earnings statements;
(13) Similar financial information for that part of the two preceding fiscal years as the issuer or its predecessor has been in existence;
(14) Whether the broker or dealer or any associated person is affiliated, directly or indirectly, with the issuer; and
(15) Whether the quotation is being submitted or published directly or indirectly on behalf of the issuer, or any director, officer, or any other person, directly or indirectly the beneficial owner of more than ten percent of the outstanding units or shares of any equity security of the issuer, and, if so, the name of such person, and the basis for any exemption under the federal securities laws for any sales of such securities on behalf of such person.[126]

This information must be reasonably current and "publicly available."[127] Generally, "publicly available" means that the information should be available on a continuous basis to such people as security holders, market makers and brokers.[128] The information disclosed is analogous to the information that must be furnished pursuant to Rule 144A.[129]

II. RULE 144A

Section 4(2), Regulation D and Rule 144 have all provided foreign issuers some access to United States domestic investors. Nevertheless, their usefulness to foreign issuers in raising capital has been limited by the number of investors, holding periods and similar restrictions applicable under those exemptions.[130] Alternatively, a

126. *Id.* at § 240.15c2-11(a)(5).
127. 17 C.F.R. § 230.144 (1990).
128. *Id.*
129. *See* Securities Act Release No. 6862, *supra* note 3.
130. *See* Panel Discussion, *supra* note 20. Foreign issuers have traditionally been reluctant to enter the domestic capital markets. The circumstances in which restricted securities (*e.g.*, those that were originally privately placed) could be resold without registration were unclear. Rule 144A clarifies the circumstances in which such securities can be resold. Pursuant to Rule 144, securities could be resold after holding them for two years (with restrictions and conditions on the manner of resale) or three years (without restrictions). 17 C.F.R. § 230.144(d). Alternatively, securities may be resold privately in reliance upon a hybrid exemption known as § 4(1-1/2). Section 4(1-1/2) relies on the exemption from registration provided by §§ 4(1) and 4(2). Section 4(1) permits sales by persons other than issuers, dealers or underwriters. Determining who is an "underwriter," the exemption draws on factors used to determine whether a distribution has occurred under § 4(2). This method of resale typically involves some holding period, a letter of investment intent by the buyer and counsel's opinion. J.W. HICKS, *supra* note 72, at 204, 305. Significantly, as documentation under a Rule 144A

United States public offering of a foreign issuer's securities is frequently not economically viable.[131] Rule 144A is designed to stimulate the secondary market for the resale and purchase of securities placed pursuant to a private placement exemption and provide foreign private issuers with an affordable and effective, albeit indirect, means to sell their securities in the United States.[132]

Again, Rule 144A is not applicable to the issuer, but to the purchaser of the issuer's securities and certain institutional buyers to whom such purchaser may resell the issuer's securities.[133] Issuers are, however, given the opportunity to indirectly expand their offering. For example, the resale market created by Rule 144A does not limit the number of qualified persons that may purchase eligible foreign securities.[134] Indirectly, a foreign private issuer will have a larger market in which to distribute its securities.[135] Additionally, a foreign private issuer theoretically will be able to more easily place its securities because purchasers that rely on a private placement exemption

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transaction becomes standardized, the delay in time associated with the registration process will be avoided and these transactions may prove to be a quick means of raising capital as compared to prior secondary market activities.

131. *See* Bush, Fin. Times, *supra* note 10, at 5. Foreign issuers are reluctant to offer their securities in the United States because public offerings require costly registration with the SEC and financial statements and related financial disclosure. Differences in accounting principles, auditing standards and auditor independence standards exist between the foreign issuer's home jurisdiction and generally accepted accounting principles [hereinafter GAAP]; reconciliation of financial statements to GAAP is required for public offerings. This can be time consuming and costly. Foreign issuers must also comply with domestic auditing requirements. This, too, can be costly and may not be possible if not done previously. Foreign issuers have also expressed concern with the liabilities imposed by American securities law and with submission to the jurisdiction of the SEC. *See* Panel Discussion, *supra* note 20. These concerns may lessen as home country markets mature, home country regulatory bodies become more active and mutual surveillance and enforcement agreements are developed and used. In addition, private offerings in the United States have not been attractive to foreign issuers because of the "illiquidity premium." *See supra* note 23.

132. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 5-1; *New U.S. Securities Rule Threatens Euromarkets, Bankers Say*, Reuters Financial Report, June 1, 1990. "Prior to Rule 144A, foreign issuers could not easily enter the U.S. market without disclosing more than they were required to in their home countries." Berkeley & Minarick, *New Rule 144A: Institutional Trading of Privately Placed Securities*, in ADVANCED SECURITIES LAW WORKSHOP 1990 69 (Practising Law Institute Handbook No. 703 1990) [hereinafter Berkeley & Minarick]. These issues avoided the domestic market as a result of stringent disclosure requirements and potential liability under securities laws. *Id.* Also gone may be premium payments previously paid with respect to illiquid securities. *Id.* at 70.

133. *See* Rule 144A, *supra* note 31.

134. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 5-21. As previously noted, an initial private offering structured for the immediate resale of the restricted securities to an unlimited number of qualified investors does not effect the initial private placement, nor the exemption available pursuant to Rule 144A.

135. *Id.*

may be more willing to invest in such securities knowing that they have other buyers to whom they can sell pursuant to Rule 144A. Furthermore, institutional secondary market buyers may more readily purchase the securities in reliance on the safe-harbor created by Rule 144A.[136]

Rule 144A is structured basically in three parts.[137] The first part sets forth the criteria to qualify as an eligible buyer.[138] The second part defines which securities are eligible to be traded in reliance on Rule 144A.[139] The third part sets forth informational disclosure requirements.[140] As a whole, the Rule's structure creates a closed secondary market of qualified buyers investing in certain securities subject to certain information being furnished to: (i) the seller of the privately placed securities concerning the buyer to determine the buyer's eligibility to participate in this closed market and (ii) the qualified buyer, in certain cases, regarding the foreign issuer to enable the qualified buyer to evaluate the investment risk.[141]

An initial step in a Rule 144A transaction may be to establish whether the institutional buyer is qualified. The person who is reselling the foreign private issuer's securities, or any person acting on his behalf must reasonably believe such buyer (i.e., a foreign bank) is eligible to participate in the transaction, pursuant to the criteria set forth in the Rule.[142] The seller can reach this conclusion by relying on certain public information or data about the buyer.[143]

A. Eligible Institutions

As previously mentioned, the Rule 144A exemption is available to institutions that are "qualified institutional buyers" under the Rule.[144] For purposes of Rule 144A, a qualified institutional buyer is

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136. *Id.*

137. Rule 144A, however, does not eliminate compliance with applicable state securities laws (Blue-Sky laws), the Exchange Act and Investment Act. It also does not remove sales made under the Rule from being subject to the anti-fraud and civil liability provisions of federal securities laws, other than §§ 11 and 12 of the Securities Act which relate to violations in connection with an issuer's registration statement. *See* Securities Act Release No. 6862, *supra* note 3. The SEC also suggested certain Rule 144A transactions could conceivably be subject to Rule 10b-6 under the Exchange Act, which prohibits any person participating in a "distribution" from bidding or purchasing on a security being distributed. *See id.*

138. Rule 144A, *supra* note 31.

139. *Id.*

140. *Id.*

141. *Id.*

142. Rule 144A, *supra* note 31.

143. *Id.*

144. *Id.* As discussed in Part IV, a buyer which is permitted to use PORTAL must

any institution that has assets invested in securities whose value attains a certain amount in terms of United States Dollars (Assets Test) for its own account or the account of other qualified institutional buyers.[145] For a foreign bank and savings and loan association or their equivalent, the threshold amount is reached if, in the aggregate, it owns and invests on a discretionary basis at least $100,000,000 in securities of issuers that are not affiliated with the institution.[146]

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demonstrate its qualifications as a buyer to the administrators of PORTAL; however, a seller should not rely on this as evidence that the institution is a qualified institutional buyer. *See* Rothwell, *The New Market for Institutional Trading: The Portal Market*, in PRIVATE PLACEMENTS AFTER RULE 144A: A SATELLITE PROGRAM 189 (Practising Law Institute Handbook No. 705 1990) (quoting PORTAL regulations) [hereinafter Rothwell]; *see also* H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 6-14.

145. Rule 144A, *supra* note 31. In addition, a potential qualified buyer may only purchase securities under Rule 144A for its own account or the account of other qualified institutional buyers. As a result, banks may not purchase for the accounts of unqualified clients. Because of the exclusion of trusts from the definition of qualified institutional buyers, banks may not purchase securities under the Rule for trust accounts.

146. *Id.* For the following entities, the threshold amount is reached if that entity, in the aggregate, owns and invests on a discretionary basis at least $100,000,000 in securities of issuers that are not affiliated with the entity:

1. *Banks*, as defined in § 3(a)(2) of the Act;
2. *Savings and Loan Associations* or other institutions, as referenced in § 3(a)(5)(A) of the Act;
3. *Foreign banks and Savings and Loan Associations* or their equivalent, foreign bank means any entity as defined by Rule 6c-9(b)(2) and (3) under the Investment Company Act of 1940 (40 Act);
4. *Insurance Companies*, as defined in § 2(13) of the Act;
5. *Investment Companies*, registered under the 40 Act (or any investment company that is part of a family of investment companies, subject to further Rule 144A requirements not discussed herein) or any business development company, as defined in § 2(a)(48) of the Act;
6. *Plans* established and maintained by a State for the benefit of its employees;
7. Employee benefit plans within the meaning of Title I of the Employee Retirement Income Security Act of 1974;
8. *Business development companies*, as defined in § 202(a)(22) of the Investment Advisors Act of 1940 (IAA);
9. *Organizations described in § 501(c)(3)* of the Internal Revenue Code of 1986, as amended, corporations (other than a bank, Savings and Loan Association, Foreign bank or Foreign Savings and Loan Association or equivalent institution), partnership, or Massachusetts or similar business trust; and
10. *Investment Advisors* registered under the IAA. For broker-dealers registered under the Exchange Act, the Rule sets out a separate, lower threshold under the Assets Test. Generally, a broker-dealer may qualify as qualified institutional buyers, for purposes of the Rule, if it owns and invests in the aggregate on a discretionary basis at least $10,000,000 in securities of issuers that are not affiliated with such dealer. The Commission has set this lower standard to enable such dealers to act as intermediaries and increase the efficiency of the market. *Id.* Notwithstanding this lower threshold, broker-dealers may act as "riskless principals" for identified qualified institutional buyers and be deemed qualified institutional buyers. A riskless principal transaction means a transaction where a dealer makes a

In addition, there is a separate net worth test that foreign banks and savings and loan associations or their equivalent must meet.[147] Such institutions wishing to trade in securities under this exemption must demonstrate a net worth of at least $25,000,000 (Net Worth Test), as set forth in their latest published audited annual financial statements.[148]

To determine whether a buyer is eligible to participate, the seller may evaluate whether an institution's audited Net Worth is equivalent to or exceeds $25,000,000 by examining the institution's books at any time within eighteen months prior to the date the issuer's securities are scheduled to be resold.[149] A foreign bank's audited Net Worth is determined by reference to the amount of equity capital shown on its most recently prepared balance sheet, prepared in accordance with generally accepted accounting principles (GAAP) and/or accounting principles mandated by law or regulation for banks in the jurisdiction of its organization or incorporation.[150]

The SEC chose these figures in the belief that a banking corporation meeting the Assets Test and the Net Worth Test has the requisite sophistication and experience to invest in such securities without the protection of certain applicable securities laws.[151] However, certain otherwise eligible banks may not be able to meet the Assets Test because Rule 144A restricts certain types of securities from inclusion in calculating the amount of securities owned or invested by the banks for purposes of the Assets Test.[152] This restriction, in conjunction with applicable banking laws, may prevent many sophisticated foreign banks from participating in this new market.[153]

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contemporaneous purchase and offsetting sale of a security from any person (excluding the issuer) to a qualified institutional buyer, including another dealer acting as a riskless principal on behalf of any qualified institutional buyer.

The list above, in general, identifies the persons eligible to use the Rule 144A resale exemption. The Rule, however, goes farther than limiting the persons eligible to use the exemption and limits the type of security which may be offered and resold under the Rule. *See id.*

147. *Id.*

148. Rule 144A, *supra* note 31. The Net Worth of a bank is its equity capital as presented in its audited balance sheet. For savings and loan associations, its Net Worth is its adjusted core capital as presented on its audited balance sheet. *See* Berkeley & Minarick, *supra* note 132, at 54. The Net Worth Test does not apply to broker-dealer affiliates of any bank or savings and loan associations. *Id.* at 55.

149. Rule 144A, *supra* note 31.

150. *Id.*

151. *See* Securities Act Release No. 6862, *supra* note 3.

152. *Statutes of Variable Rate Demand Notes Use Loans as Security*, Investment Securities Letter No. 3 [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,873 (July 17, 1986) [hereinafter *Statutes of Variable Rate Demand Notes*].

153. *Id.*

There has been criticism of subjecting banks, unlike other eligible institutions, to the Net Worth Test. Some commentators question whether the number of available investors qualified as buyers under current Rule 144A criteria would be sufficiently large to provide adequate liquidity to the market.[154] Furthermore, the $25,000,000 figure seems arbitrarily chosen as a measure of sophistication. Arguably, other less capitalized banking institutions may be sufficiently sophisticated to fend for themselves. Nevertheless, with the gradual erosion of applicable banking law prohibitions in securities trading, it may be prudent to subject banks to a separate investment sophistication test given that banks in a deregulated industry may be investing depositors' funds (as opposed to their own funds). Moreover, the integrity of the banking system must be maintained.

B. Eligible Securities

Rule 144A applies to "restricted securities,"[155] but the Rule limits the availability of the safe-harbor to specific types of restricted securities,[156] based on criteria provided in the Rule.[157] Ultimately, the SEC's discretionary characterization of the securities determines whether the securities are eligible.[158]

As provided in the Rule, the exemption is not available to an offer or sale of securities that, at the time of issuance, is of the "same class" of the issuer's securities currently listed on a United States securities exchange or quoted on an automated inter-dealer quotation system (Securities Test).[159] Under the SEC's "same class" test, common equity securities that are substantially similar in character, which provide their holders with substantially similar rights and privileges, as listed shares will be deemed of the same class with the listed shares.[160] The Rule seeks to prevent evasion of the registration and disclosure requirements of the Securities Act by preventing "identical" securities of the issuer's then-issued securities from entering the private market concurrently with such publicly traded securities.[161]

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154. *See* Berkely & Minarick, *supra* note 132, at 75.

155. Rule 144A, *supra* note 31.

156. *Id.*

157. *Id.*

158. *Id.* The SEC release with respect to Rule 144A defines criteria for determining whether an issuer's securities are of the "same class" as previously issued securities. A no action letter may be sought if some doubt exists as to whether the new issuance is of the same class as a prior issuance. The SEC's descretion would determine the securities' eligibility.

159. Rule 144A, *supra* note 31.

160. Securities Act Release No. 6862, *supra* note 3.

161. *Id.*

An automatic quotation system includes quotation on the National Association of Securities Dealers Automated Quotation system (NASDAQ), but would exclude bid and ask quotations in the current "pink sheets" of the National Quotation Bureau, Inc. and securities quoted on PORTAL.[162]

Preferred capital stock providing rights and preferences, including a dividend rate, cumulation, participation, liquidation preference, voting rights, convertability, call, redemption and other material matters, that are substantially similar in character as the issuer's currently listed shares will be deemed to be of the same class as the listed shares.[163] Likewise, debt securities will be deemed of the same class if their interest rate, maturity, subordination, security, convertability, call, redemption and similar material matters are substantially identical to listed debt securities.[164]

The Rule sets out special provisions governing the evaluation of: (i) securities that are convertible into listed securities and (ii) warrants that may be exercised for listed securities.[165] Under the Rule, a convertible security is to be treated as both the convertible and the underlying listed security unless, at issuance, it had an effective conversion premium (ECP) of at least ten percent.[166] If the ECP is less than ten percent, the convertible security will not be deemed of the same class as the security into which it is convertible.[167]

Similarly, warrants will be deemed securities of the same class as the underlying listed security if, at issuance, they are exercisable for a period of less than three years or have an effective exercise premium (EEP) of at least ten percent.[168] The EEP is determined in roughly

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162. *Id.*

163. Securities Act Release No. 6862, *supra* note 3.

164. *Id.*

165. *Id.*

166. Securities Act Release No. 6862, *supra* note 3. The ECP, expressed in monetary terms, is the securities price at issuance less its conversion value (the aggregate market value of the securities that would be received upon conversion). The ECP is expressed as a percentage of the conversion value. The conversion value is determined by reference to the market price of the listed security on the day the convertible security was priced. The market price of the underlying security may be determined by reference to any bona fide sale price in a transaction occurring on a United States securities exchange or NASDAQ on the day of pricing of the convertible security. For example, if a $1,000 bond is convertible into 25 shares of common stock, and the bond is issued at par (i.e., $1,000), and the market price of the common stock is $35 on the day the bond is priced (i.e., the conversion value is $875, the product of $35 multiplied by 25), then the ECP would be 14.29% ($125 [obtained by subtracting $875 from $1,000] as a percentage of $875). *Id.*

167. *Id.*

168. Securities Release Act No. 6862, *supra* note 3.

the same manner as the ECP.[169]

Finally, the Rule 144A exemption is not available for American Depository Shares (ADSs) listed on a United States exchange or quoted on NASDAQ. The deposited securities represented by the ADSs are deemed publicly traded; therefore, the ADSs would be characterized as of the same class as the deposited securities.[170]

Unfortunately, the breadth of these conditions may exclude common stock from eligibility and relegate the Rule's use to nonconvertible debt and nonconvertible preferred stock.[171] This may endanger the newly created secondary trading market in equity securities on PORTAL.[172]

The Securities Test was included in response to concerns that, without it, foreign private issuers might opt for trading their securities pursuant to Rule 144A rather than continue to offer them in the pub-

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169. *Id.*

170. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 6-4. An example of successful equity placement in reliance on Rule 144A has been American Depositary Receipts (ADRs). ADRs are "negotiable receipts issued by a United States bank or trust company (Depository) to evidence ownership of securities of a foreign company deposited with the Depository's office or agent in the foreign country." ADRs are considered separate securities from the underlying foreign security and are subject to separate federal securities laws, except for purposes of Rule 144A. ADRs are exempt from registration and the SEC requires the issuer to file only Form F-6. Form F-6 is a limited voluntary disclosure statement. Foreign issuance of ADRs have several distinct advantages. These include efficient settlement procedures, conversion of dividend payments into American dollars and Depository monitoring of Rule 144A compliance. The Depository may also provide the information to qualified institutional buyers conditioned in a Rule 144A transaction. Zaitzeff, *supra* note 38, at 30.

In June of 1990, the Swedish manufacturing and distribution company, Atlas Copco AB, made a two tranche offering of its securities in the international and United States market. Atlas Copco raised £125,000,000 with its offering and placed 20-25% of its shares in the United States and was the first private placement of equity under Rule 144A. The Company's shares were divided into two classes consisting of "A shares" and "B shares" which were deemed of the "same class." The company issued approximately 4,000,000 A shares outside Sweden; one tranche of shares was issued in the European securities market and was resold in part through the International Stock Exchange of the United Kingdom and the Republic of Ireland Limited. The second tranche, consisting of approximately 1,000,000 B shares, resold in the United States in the form of American Depository Shares (ADSs), with three B shares represented by one ADS. The ADSs were traded on PORTAL. *See* Ford, *Private Placements After Rule 144A*, in PRIVATE PLACEMENTS AFTER RULE 144A: A SATELLITE PROGRAM 75 (Practising Law Institute Handbook No. 705 (1990)) [hereinafter Ford].

The B shares, however, were not listed on a United States exchange or quoted on NASDAQ. *Id.* The number of companies without publicly traded common stock that might use an offer exemption like Rule 144A is small.

171. *See* H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 6-22. In April 1990, Moody's Investors Services, Inc. predicted that a two-tiered market would be created. One tier represented the traditional illiquid private placements market and the other tier representing issuances in the public market such as high quality, debt instruments. *See* Quinn, *supra* note 14, at 73.

172. *See infra* notes 255-259.

lic market. Such a situation would have created a two-tier market with trading in the same security.[173] Some commentators to the SEC's proposed Rule 144A felt that this alleged diversion from the public market would result in "reduced liquidity, differential pricing and volatility" in the public market.[174] The breadth and effect of this exclusion, in comparison to the harm it seeks to prevent, may not warrant its inclusion in Rule 144A.

A reduction in liquidity is improbable.[175] Presumably, a reduction would occur as a result of the removal of a significant portion of an issuer's securities from the public market.[176] This presupposed flight of foreign issuances in capital stock from the United States public market ignores the fact that the issuer must undertake a private placement of its securities to qualify such securities for trading on PORTAL, as discussed in Part I of this Article.[177] The motivation

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173. *See SEC Rule 144A: A New Market*, *supra* note 20. It has been suggested that if a two-tiered market is created it will be one of institutional investors under Rule 144A and smaller investors ineligible to participate under the Rule. Quinn, *supra* note 14, at 73.

174. *See* Hanks, *Background to Rule 144A*, in PRIVATE PLACEMENTS AFTER RULE 144A: A SATELLITE PROGRAM 10 (Practising Law Institute Handbook No. 705 (1990)) [hereinafter Hanks]. On October 25, 1988, the Commission issued Securities Act Release No. 6806, proposing in Rule 144A a safe-harbor exemption from the Securities Act registration requirements for specified resales of securities to institutional investors. The original version proposed three "tiers." The first tier would permit any security to be resold to institutions with $100,000,000 in assets, while the other two tiers would have permitted a more restricted group of securities to be resold to institutions with $5,000,000 in assets. A number of commentators urged the Commission to proceed cautiously by adopting the Rule in stages. Most commentators suggested a staged phase-in of the Rule proceeding initially by making Rule 144A available to large institutional buyers. Several suggested that a definition of "qualified institutional buyer" linked to securities investments would provide a better test of an institution's investment sophistication than the proposed total assets test. The SEC had requested comment on the likelihood that, under Rule 144A, an active, liquid private market would develop alongside a public market in the United States for the same class of securities (side-by-side trading). Commentators responding to this question were divided, some concurred with the Commission's view that significant side-by-side markets were unlikely to develop. Others, however, stated that the proposed Rule might have the effect of diverting some securities away from the public market to the private market and expressed concern that the public markets and investors in these markets might be disadvantaged by resulting reduced liquidity, differential pricing and volatility. Some commentators also expressed the position that the Rule would decrease the quality and quantity of securities available to retail investors. *Id.*

175. Quinn, *supra* note 14, at 73; *Sec Rule 144A: A New Market*, *supra* note 20. "As a practical matter, many forms of debt geared to institutional markets differ markedly from publicly traded debt. Similarly, preferred stock placed with institutional investors generally is different in formulation from preferred stock offered to the public." *Id.* However, common stock traded on PORTAL would be the same as common stock traded on an exchange. Even trading in common stock on PORTAL would probably not result in flight from the domestic exchanges. *See* H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 6-22.

176. *See* H. BOOMENTHAL (1990 ed.), *supra* note 2, at 6-22.

177. *See id.*

and purpose for undertaking a private offering are often quite different from those which cause an issuer to undertake a public offering.[178] A public offering is just that, an offering, and its success in raising capital, in part, is attributable to investor confidence in the security. The stronger the issuance, the greater the public's purchase of the securities and the more capital is raised. A private issuance usually involves a purchase transaction by a limited number of buyers. These privately placed securities are restricted securities[179] and the purchaser of such a security generally must assume the economic/investment risk in buying the security, thus limiting the market for privately placed securities. The ramifications and the complexity associated with undertaking a private placement make it unlikely that a foreign private issuer would avoid registration by utilizing a private placement to trade securities on PORTAL.

In addition, a substantial private offering may be limited to a specific number and type of buyers and require disclosure of the same information required by registration under the Securities Act.[180] The SEC's rules on integration prevent evasion through consecutive offerings.[181] Consequently, a clear advantage may not be gained by a foreign issuer seeking to avoid the cost and intrusive disclosure requirements associated with registering its shares under the Securities Act.[182]

Furthermore, a foreign issuer is not legally prohibited from offering any portion of its publicly traded securities and can privately place them with any number of accredited investors.[183] Accredited investors, with their requisite sophistication, are deemed capable of assessing the investment risk in the purchase of securities.[184] These investors may effect further private resales to other accredited inves-

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178. In both a public and private offering the issuer seeks to raise capital. Private placements, however, tend to be negotiated transactions rather than offerings. A significant public offering can tend to divest or dilute ownership of a company, while a private offering may be more narrow in focus.

179. 17 C.F.R. § 230.502 (1990); H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 5-23. Foreign private issuers are wary about effecting a private placement because they are concerned with the complexity of a Regulation D offering and restrictions on resales. *Id.*

180. *See supra* notes 54-95 and accompanying text.

181. 17 C.F.R. § 230.502 (1990).

182. The foreign private issuer's cost is often associated with the difficulty of disclosure requirements. *See supra* notes 129 and 130 and accompanying text. Additionally, the aims of a private placement and a public offering do not correspond.

183. *See supra* notes 54-95 and accompanying text.

184. Generally, persons that qualify as accredited investors may not qualify as qualified institutional buyers. *See supra* note 145 and accompanying text. *See also supra* notes 83 and 84 and accompanying text.

tors.[185] In effect, this creates a private and public market in the same security, with no appreciable impact on the liquidity of the public market.

The "same class" prohibition also ignores post-registration requirements or filing by a foreign issuer of its home country informational filings with the SEC.[186] These requirements and limitations may discourage flight from the public market.[187]

Price-differentiation is presumed to occur if a side-by-side market exists in the same security.[188] One market would reflect a different value for the particular security than the other.[189] A share's price is, however, a reflection of the market's belief in the value of a share of stock in a particular corporation in relation to other economic and political factors.[190] Both markets would base their price on the same publicly available information.[191] Theoretically, the price of a share in one market should not be different than the price of such share in the other market.[192] In addition, the modified holding periods of Rule 144 will facilitate the entrance of securities traded on PORTAL into the public market. Also, foreign-issued securities may be resold in the issuer's home jurisdiction pursuant to Regulation S.[193] As a result, equity securities traded on PORTAL will not be isolated from the public market.[194] It is likely that side-by-side trading of fungible securities on PORTAL with securities of the same class on a national exchange or NASDAQ will not result in price differentiation of the shares on the different markets or create volatility in such markets.

C. Disclosure

1. Disclosure with Respect to Qualified Institutional Buyers

As previously mentioned, to rely on Rule 144A, the seller and any person acting on its behalf must reasonably believe that the pro-

185. *See* 17 C.F.R. § 230.506 (1990).

186. *See infra* notes 424-434 and accompanying text.

187. *Id.*

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

189. *Id.*

190. *See* Garten, *supra* note 77, at 540-47.

191. The "same class" prohibition assumes that the common stock is already traded publicly and that, therefore, the information disclosed in connection with the issuer's previously issued common stock would be available to the qualified institutional buyer.

192. Banking Rep. (BNA), vol. 54, No. 23, at 998 (June 11, 1990). *See infra* note 362 and accompanying text.

193. Rule 144A, *supra* note 31. Securities Act Release No. 6863, *supra* note 6.

194. *Id.*

spective purchaser is a qualified institutional buyer.[195] The seller or any person acting on the seller's behalf may rely on certain sources of information. This information concerns the amount of securities owned and invested on a discretionary basis by a prospective purchaser, including a foreign bank investing in securities in the resale market, to establish whether the institution meets the eligibility requirement to qualify as a qualified institutional buyer. This information must be current (within the eighteen month period previously mentioned) and include:

1. The institution's most recent publicly available annual financial statements;
2. The most recent information appearing in documents filed by the prospective purchaser with the SEC or another United States federal, state, or local governmental agency or self-regulatory organization, or with a foreign governmental agency or foreign self-regulatory organization;
3. The most recent information appearing in a recognized securities manual (i.e., Moody's publications or their equivalent); and
4. Certification by the institution's chief financial officer, or another executive officer, unless the seller knows of any misrepresentation therein, specifying the threshold amount as of a specific date on or since the close of the institution's most recent fiscal year.[196]

The seller and any person acting on its behalf would be able to rely on the foregoing information to establish an institution's eligibility to participate in the resale market pursuant to Rule 144A notwithstanding the existence of other, more current information that may show a lower amount of securities owned by the institution.[197] The seller is permitted to establish a reasonable belief of eligibility based on factors other than those stated above.

2. *Disclosure with Respect to the Foreign Issuer*

Where the foreign issuer is a reporting company under the Exchange Act, the seller does not have to provide information to the prospective purchaser.[198] For foreign private issuers that do not file periodic reports with the SEC under the Exchange Act or foreign pri-

195. Rule 144A(d)(1), *supra* note 31.

196. *Id.*

197. *See* Securities Act Release No. 6862, *supra* note 3.

198. *Id. See also SEC Rule 144A: A New Market*, *supra* note 20. However, a difficulty for a foreign private issuer is that its privately placed securities may quickly flow back to its home market since the offering is not supported by adequate information disclosure. Fin. Times, July 2, 1990, at 3. A company may have to balance its interest between confidentiality versus disclosure to enhance trading in its security.

vate issuers that do not provide home country information to the SEC, the safe-harbor of Rule 144A will be conditioned generally on: (i) the security holder or prospective purchaser designated by the holder having the right to obtain upon request certain basic financial information from the foreign private issuer and (ii) the prospective purchaser being sent the information at, or prior to, the time of sale, upon the purchaser's request to the holder or the issuer.[199] This information includes:

1. A brief statement on the nature of the issuer's business and of its products and services offered as of twelve months prior to the date of resale.[200]
2. A balance sheet dated less than sixteen months prior to the resale, and statements of profit and loss and retained earnings for the twelve months preceding the date of the balance sheet.[201] If the balance sheet is dated six months or more prior to the resale, an additional statement of profit, loss and retained earnings for the period from the date of the balance sheet to a date less than six months prior to the resale date, must accompany the balance sheet.[202]

The financial statements of the foreign private issuer should be audited if audited financial statements are readily available, but there is no requirement that they conform to the SEC's accounting rules.[203] Furthermore, information provided by a foreign private issuer must only meet the timing requirements of the issuer's home country or principal trading markets.[204]

Information furnished by an institution wishing to participate as a qualified institutional buyer, or information provided by a non-reporting foreign private issuer, is not considered burdensome or intrusive.[205] The cooperation of non-reporting foreign private issuers, however, is essential to insure that the Rule 144A safe-harbor remains.[206]

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199. *See* Securities Act Release No. 6862, *supra* note 3.

200. *Id.*

201. *Id.*

202. *Id.*

203. *See* Securities Act Release No. 6862, *supra* note 3.

204. *Id.*

205. Fin. Times, May 3, 1990, at 14. A path is cleared for foreign issuers to participate in the domestic securities market. The information will be relatively "easy to provide" since it is similar to information already available in its home country. *Id.*; H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 5-31.

206. *See supra* note 198 and accompanying text. "The required information can be obtained only with the cooperation of the issuer. This [requirement] could be contractually [set

III. REGULATION S

Regulation S regulates unregistered offshore offerings.[207] It defines the parameters under which an offering may take place outside the United States without being subject to registration under the Securities Act.[208] Rule 144A provides a safe-harbor for offerings made within the United States including securities originally offered in a Regulation S offshore offering.[209] Regulation S also allows qualified institutional buyers to resell restricted securities acquired through PORTAL to any foreign market where shares are traded.[210] Adoption of Regulation S may enhance the liquidity of the Rule 144A private placement market and facilitate active trading in equity securities on PORTAL and abroad.[211]

Prior to the advent of Regulation S, the SEC formulated a series of directives designed to prevent resale of unregistered foreign-issued securities distributed primarily in foreign markets to unsophisticated investors in the United States.[212] Release No. 33-4708 operated as the principal means of determining whether securities issued by a foreign issuer in a foreign country had to be registered with the SEC.[213] Generally, any foreign offering that met the SEC's criteria was not subject to registration in the United States.[214] For securities involved in an offshore foreign issuance,[215] the SEC required the issuer to include mechanisms in its offering to prevent impermissible resales to United States citizens.[216] These mechanisms, commonly called "anti-flowback" provisions, usually contained the following provisions:

(a) A prohibition on sales to United States nationals, including United States citizens and resident aliens;

(b) A representation that the foreign investor is purchasing the se-

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forth] in a new private placement . . . assuming no undue expense or liability [on the part of the issuer]." *SEC Rule 144A: A New Market*, *supra* note 20.

207. 17 C.F.R. §§ 230.901-904 (1990).

208. *Id.*

209. Rule 144A(e), *supra* note 31.

210. 17 C.F.R. § 230.904 (1990).

211. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 7-64.

212. *See id.* at 7-12; Note, *Foreign Securities Offerings in the United States: The Impact of SEC Clearance of Denationalized French Stock Issues*, 21 VAND. L. REV. 549, 587 (1988) [hereinafter Note, *Foreign Securities Offerings*].

213. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 7-12.

214. See Quinn, *supra* note 14, at 35.

215. For domestic privately-held shares the § 4(1-1/2) exemption of the Securities Act enabled the resale of privately placed securities under United States law. *See* J.W. HICKS, *supra* note 72, at 475.

216. *See* H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 7-12.

curities for its own account and not for the account of a United States national;

(c) A representation that the underwriters and investors will not resell the securities in the United States or to United States residents;

(d) A ninety day restriction on the transfer of the subject securities after the conclusion of the foreign offering;

(e) A prohibition on the resale of the securities in the United States or to United States nationals after the ninety day period;

(f) A requirement that the prospectus include a legend representing that the offered securities have not been registered with the SEC; and

(g) A requirement that the issuer's transfer agents be instructed to stop any transfer which violates or is not in compliance with anti-flowback transfer restrictions.[217]

Under Release No. 33-4708, many issuers were unsure what anti-flowback mechanisms to include in their offerings and securities professionals were unsure whether the same mechanisms applied to all types of securities.

Regulation S, however, takes the guessing game out of structuring an exempt offshore transaction and incorporates many of the anti-flowback provisions of Release No. 33-4708.[218] Regulation S includes two safe-harbors.[219] One applies to offerings by issuers (Issuer Offering) and the other applies to resales by persons other than the issuer (Non-Issuer Offering).[220] With respect to these two offerings, Regulation S sets forth three criteria to determine if the offer occurred outside the United States.[221] These provisions include:

1. the offer or sale must not have taken place within the United States, including its territories and possessions;[222]
2. the offer or sale of securities is made in an "offshore transaction";[223] and

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217. *See id.* These terms generally reflect the provisions that relate to debt instruments. The SEC suggested implementation of anti-flowback provisions to make sure securities came to rest abroad, depending on whether the instrument was a debt or equity security. *See* Quinn, *supra* note 14, at 35. The SEC confirmed that equity securities would be considered to have come to rest abroad if no transfer to American residents occurred 12 months after the offering, and then only if such securities were registered or exempt, and a restrictive legend was placed in the share certificate and prospectus. *See id.* at 38.

218. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 7-64.

219. *See* Securities Act Release No. 6863, *supra* note 6, at 13.

220. *Id.*

221. *Id.*

222. *See id.*

223. *Id.* 17 C.F.R. § 230.902(i)(1) (1990). An offer or sale of securities is made in an "offshore transaction" if:

3. no "directed selling effects" are made in the United States by the foreign issuer,[224] a distributor[225] or an affiliate.[226]

Regulation S sets forth additional criteria for an Issuer Offering and distinguishes three categories of securities offerings by a foreign issuer based on "factors such as nationality and reporting status of the issuer, and the degree of United States market interest in the issuer's securities."[227] The first category includes foreign issuers with no substantial United States market interest.[228] The second category in-

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(i) the offer is not made to a person in the United States; and (ii) either: (A) at the time the buy order is originated, the buyer is outside the United States, or the seller and any person acting on its behalf reasonably believe that the buyer is outside the United States; or (B) for purposes of: (1) § 230.903, the transaction is executed in, on or through a physical trading floor of an established foreign securities exchange that is located outside the United States; or (2) § 230.904, the transaction is executed in, on or through the facilities of a designated offshore securities market described in paragraph (a) of this section, and neither the seller nor any person acting on its behalf knows that the transaction has been pre-arranged with a buyer in the United States.

224. 17 C.F.R. § 230.902(f)(1) (1991). " 'Foreign issuer' means any issuer that is: (i) foreign government; (ii) national of any foreign country; or (iii) corporation or other organization incorporated or organized under the laws of any foreign country."

225. *Id.* at § 230.902(c). " 'Distributor' means any underwriter, dealer, or other person who participates, pursuant to a contractual arrangement, in the distribution of the securities offered or sold in reliance on this Regulation S."

226. *Id.* at § 230.902(b)(1).

'Directed selling efforts' means any activity undertaken for the purpose of, or that could reasonably be expected to have the effect of, conditioning the market in the United States for any of the securities being offered in reliance on this Regulation S. Such activity includes placement of an advertisement in a publication with a general circulation in the United States that refers to the offering of securities being made in reliance upon this Regulation S.

(2) Notwithstanding paragraph (b)(1) of this section, placement of an advertisement required to be published under United States or foreign law, or under rules or regulations of a United States or foreign regulatory or self-regulatory authority, shall not be deemed 'directed selling efforts,' provided the advertisement contains no more information than legally required and includes a statement to the effect that the securities have not been registered under the Act and may not be offered or sold in the United States (or to a United States person, if the advertisement relates to an offering under § 230.903(c)(1) or (3)) absent registration or an applicable exemption from the registration requirements. . . .

"Additionally, a tombstone advertisement in a publication with a general circulation in the United States shall not be deemed 'directed selling efforts,' provided: (i) The publication has less than 20% of its . . . circulation in the United States; (ii) [Such advertisement contains a restrictive legend]; and (iii) [Such advertisement contains only limited information about the issuer and the offspring]." *Id.* at § 230.902(b)(4).

227. 17 C.F.R. § 230.902 (1991); *see also* Securities Act Release No. 6863, *supra* note 6.

228. 17 C.F.R. § 230.902(n)(1).

'Substantial U.S. market interest' with respect to a class of an issuer's equity securities means: (i) The securities exchanges and inter-dealer quotation systems in the United States in the aggregate constituted the single largest market for such class of securities in the shorter of the issuer's prior fiscal year or the period since the issuer's incorpora-

cludes foreign reporting issuers and non-reporting foreign issuers selling certain types of stock, each with substantial domestic market interest.[229] The third category is a residuary category that includes all securities not covered by the prior two categories, including equity securities of non-reporting foreign issuers with substantial United States market interest.[230]

With respect to the first category of an Issuer Offering, no other preconditions must be met, provided: (1) the foreign issuer reasonably believes at the commencement of the offshore transaction that no substantial United States market interest exists in the class of securities offered or sold, (2) the securities are offered or sold in an overseas directed offering, (i.e., the offer is directed to a single country or to any resident of such country in accordance with its applicable law), and (3) the securities are backed by the full faith and credit of a foreign government.[231]

Regulation S also sets forth anti-flowback provisions applicable to the second category of an Issuer Offering.[232] The provisions are designed to limit unregistered public offerings in the United States during the initial offshore selling efforts. Should these offshore securities subsequently flowback into the United States, public investors of reporting foreign issuer securities will be protected by the information made available under the Exchange Act.[233] The additional preconditions include: (i) the foreign issuer must be a reporting issuer,[234] or in the case of a non-reporting foreign issuer, the securities offered must be debt securities, (ii) each underwriter must agree in writing not to offer or sell unregistered securities prior to the expiration of certain

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tion; or (ii) 20 percent or more of all trading in such class of securities took place in, on or through the facilities of securities exchanges and inter-dealer quotation systems in the United States and less than 55 percent of such trading took place in, on or through the facilities of securities markets of a single foreign country in the shorter of the issuer's prior fiscal year or the period since the issuer's incorporation.

Id.

229. 17 C.F.R. § 230.903 (1991).

230. *Id.* at §§ 230.902(n)(1) and 230.903; *see also* Securities Act Release No. 6863, *supra* note 6.

231. *Id.* at § 230.902.

232. 17 C.F.R. § 230.903.

233. *See* Securities Act Release No. 6863, *supra* note 6.

234. 17 C.F.R. § 230.902(l) (1991). "Reporting issuer" means an issuer that:

(1) Has a class of securities registered pursuant to section 12(b) or 12(g) of the Exchange Act (15 U.S.C. § 78l(g)) or is required to file reports pursuant to section 15(d) of the Exchange Act (15 U.S.C. § 78o(d)); and (2) has filed all the material required to be filed pursuant to section 13(a) or 15(d) of the Exchange Act (15 U.S.C. §§ 78m(a) or 78o(d)) for a period of at least twelve months immediately preceding the offer or sale of securities made in reliance upon Regulation S. . . .

holding periods,[235] (iii) the unregistered securities must contain a legend representing that the securities have not been registered under the Securities Act and may not be sold in the United States, (iv) the offer or sale must not be made to a United States resident, and (v) each distributor must give notice to purchasers stating that the purchaser is subject to limitations on offers and sales imposed on the distributor.[236]

With respect to category three of an Issuer Offering, Regulation S establishes preconditions that include offering restrictions. In essence, these additional preconditions are the anti-flowback provisions established under Release No. 4708. Except for equity securities, an offer to a domestic resident is prohibited if made prior to a one-year restricted period.[237]

The Non-Issuer Offering is broad.[238] Nevertheless, it does not provide a safe-harbor for resales in the United States.[239] An institution that is not a distributor or an issuer may use the Non-Issuer Offering to effect a resale of securities issued in a Regulation S offshore transaction.[240] Therefore, the Non-Issuer Offering, with Rule 144A, permits a qualified institutional buyer to resell exempt tranches of a Rule 144A offering traded on PORTAL. This can be done if the issuer resells the securities outside of PORTAL in an offshore transaction without a directed selling effort aimed at the United States market. This is true if the sale occurs in a designated offshore securities market,[241] or in the market in which the offshore tranche is sold.[242]

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235. *Id.* C.F.R. § 230.902 (m). The holding periods are "restricted periods" meaning "a period that commences on the later of the date upon which the securities were first offered to persons other than distributors in reliance upon this Regulation S or the date of closing of the offering, and expires a specified period of time thereafter. . . ."

236. *See* Securities Act Release No. 6863, *supra* note 6.

237. *Id.*

238. 17 C.F.R. § 230.904 (1991).

239. *Id.*

240. *Id.*

241. 17 C.F.R. § 230.902(a).

Designated offshore securities market means: (1) The Eurobond market, as regulated by the Association of International Bond Dealers; the Amsterdam Stock Exchange; the Australian Stock Exchange Limited; the Bourse de Bruxelles; the Frankfurt Stock Exchange; The Stock Exchange of Hong Kong Limited; The International Stock Exchange of the United Kingdom and the Republic of Ireland, Ltd.; the Johannesburg Stock Exchange; the Bourse de Luxembourg; the Borsa Valori di Milano; the Montreal Stock Exchange; the Bourse de Paris; the Stockholm Stock Exchange; the Tokyo Stock Exchange; the Toronto Stock Exchange; the Vancouver Stock Exchange; and the Zurich Stock Exchange; and (2) Any foreign securities exchange or non-exchange market designated by the [SEC].

Id.

242. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 7-44.

IV. PORTAL

Concurrently with the adoption of Rule 144A, the SEC approved a new automated quotation system called PORTAL.[243] PORTAL was created by the National Association of Securities Dealers (NASD), which developed and instituted NASDAQ.[244] PORTAL functions in much the same way as NASDAQ and was designed to encourage trading and create a fluid resale market in association with Rule 144A.[245]

A user of PORTAL must be a qualified institutional buyer.[246] In accordance with the Rule 144A requirements for establishing whether an institution is a qualified institutional buyer, PORTAL rules require users to demonstrate eligibility prior to access to PORTAL.[247] Generally, the documentation to establish eligibility to use PORTAL is similar to that required under Rule 144A.[248]

PORTAL rules also require that the securities traded on PORTAL be in negotiable form and not subject to restrictions that would burden a PORTAL participant. Furthermore, foreign issuer securities must be deposited[249] in the Centrale de Livraison de Valeurs Mobilieres, SA, Luxembourg depository.[250] In addition, investors in PORTAL traded securities must establish segregated accounts for foreign issued securities at the International Securities Clearing Corporation.[251]

As of June 1990, twenty-one broker-dealers and ten institutions had signed up to use PORTAL.[252] For users, PORTAL terminals

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243. *See* Hanks, *supra* note 174, at 17.

244. *NASD Launches New PORTAL Market; First 144A Offerings Placed Through Screen-Based System*, PR Newswire, June 18, 1990 [hereinafter PR Newswire]. PORTAL functions through NASDAQ terminals in principally the same manner. The introduction of NASDAQ in the trading of over-the-counter securities instantaneously transformed a slow market into an efficient sophisticated automated market. PORTAL's introduction did not instantaneously transform an established market because the market it automated was composed of complex debt securities ill adapted for trading on such a system. PORTAL's use will be greatest in secondary trading in equity securities that can be readily valued by market forces. *See* Panel Discussion, *supra* note 20.

245. *See* PR Newswire, *supra* note 244.

246. *See* PORTAL Market Rules, at pt. IV, § 1 (as approved by the SEC Apr. 27, 1990), *reprinted in* PRIVATE PLACEMENTS AFTER RULE 144A: A SATELLITE PROGRAM 214 (Practising Law Institute Handbook No. 705 (1990)) [hereinafter PORTAL Market Rules].

247. *Id.*

248. *Id.* A PORTAL qualified investor must demonstrate its eligibility to purchase securities in accordance with Rule 144A. *Id.* at pt. IV, § 1(b).

249. *See* PORTAL Market Rules, *supra* note 246, at pt. II, § 2(a)(2).

250. See Rothwell, *supra* note 144, at 139.

251. *Id.* at 138.

252. 1990 Institutional Investor, Inc.; *Private Placement System Eyed by NYSE*, Bank

display prices and other data on eligible, privately-placed equity and debt instruments.[253] To promote trading and facilitate Rule 144A transactions, PORTAL provides entry and retrieval of quotations, automatic confirmations to parties of resale transactions, a standard five-day settlement period and settlement by electronic book-entry.[254] PORTAL thus provides a worldwide clearing and depository system and enables qualified users to quickly quote, confirm and settle transactions in major world currencies.

As a result, PORTAL facilitates the rapid trading of securities typically associated with equity securities, in contrast with trading in debt securities.[255] Unlike other automated quotation systems, PORTAL is a closed system, open only to eligible participants trading in eligible securities.[256] This unique structure makes PORTAL's success dependent on a limited number of buyers and certain securities that meet the eligibility requirements, particularly equity securities.[257] By August 1990, only a handful of offerings in equities had occurred.

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letter, June 25, 1990, vol. X, No. 25, at 2. An estimated 60 other institutions have begun the sign-up process by the end of June 1990. *Id.*

253. *See* PR Newswire, *supra* note 244.

254. *Id.* PORTAL's international settlement procedures may encourage the globalization of securities offerings and transactions and reduce the risk of currency fluctuation during settlement. *Id.*

255. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 6-2, 6-4. Potentially, PORTAL can be convertible to accommodate other instruments such as bonds. *See* Berkeley & Minarick, *supra* note 132, at 81. To use PORTAL, a qualified institutional buyer is required to use a PORTAL broker. *Id.* at 90. As an example of a typical secondary transaction on PORTAL, a dealer will display quotation information available to PORTAL participants. The form of quotation is flexible and may be facilitated by entering a telephone number to negotiate trades. *Id.* at 86. The market will be dealer-based. *Id.* Institutions "will see on their PORTAL screens the quotes of individual dealers, but they themselves will not be able to enter quotes or deal directly with other institutions. The potential buyer will choose a dealer and negotiate a transaction. The dealer will imput a trade report of the sale, which will create a system-generated confirmation to the buyer. The buyer will enter an acceptance of the transaction, and the system will create a record for transmission to clearing." *Id.* at 87. A criticism of PORTAL requirements is that many qualified buyers do not use brokers. As a result, many eligible buyers may choose to trade outside PORTAL.

256. *See* Rothwell, *supra* note 144, at 190-205. PORTAL is closed to trading in all securities except eligible securities of a different class than the issuer's previously issued publicly traded securities by qualified institutional buyers. *Id.*

257. *Id.* Certain debt instruments are equally suited to trading on PORTAL. *See* Jiji Press Ticker Service, *Nissan to Issue Private Bonds in United States*, June 22, 1990 (reporting Nissan capital of America would be the first Japanese Company to resell corporate bonds pursuant to Rule 144A). However, most debt instruments traded in a private placement tend to have long maturities and are intended to be held long-term by a purchaser, such as an insurance company. *See* Panel Discussion, *supra* note 20. A representative of [Aetna] Insurance Company stated generally that the exemption provided by Rule 144A was not requested by insurance companies, the predominant purchasers of privately placed debt, and that the § 4(1-1/2) exemption was better and would continue to be used. However, PORTAL may

This lack of participation in PORTAL may be due in part to the Rule 144A prohibition against trading securities of the "same class" as the issuer's earlier issued publicly traded stock. As discussed in Part II of this Article, the "same class" prohibition directly limits the number of eligible equity securities which can be traded on PORTAL.[258] Consequently, a system designed to promote trading in equity securities is relegated to trading primarily in debt instruments and its success may be jeopardized by the "same class" prohibition.[259] Without PORTAL, or a PORTAL relegated to facilitating trading in debt instruments, the SEC may not achieve the intended secondary market liquidity.

In addition, as a result of the restrictions on the type of securities eligible for trading on PORTAL, foreign private issuers may not use Rule 144A to the extent anticipated. Foreign banks also will be limited in the type of security they may resell on PORTAL.

V. Foreign Banks

Foreign banks may participate in a Rule 144A transaction in a number of ways.[260] They may participate in the initial placement of a foreign private issuer's securities.[261] Traditionally, a bank's role in an issuer's private placement is limited to that of advisor to the issuer.[262] A foreign bank acting in such a role may advise as to structuring the placement, identifying investors or helping to negotiate a private placement.[263] In this capacity, foreign banks usually do not act as agents of the issuer; therefore, they cannot bind the issuer in terms of the offer.[264]

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function as a medium to facilitate securities trading and provide a means by which bank regulators can police bank activity in the market.

258. *See supra* note 170 and accompanying text.

259. H. Bloomenthal (1990 ed.), *supra* note 2, at 6-2, 6-4, 6-22.

260. *See supra* notes 130-143 and accompanying text.

261. *See generally* 5 Banking Law, Banks and Securities Law § 96.01 (1990) [hereinafter Banks and Securities Law].

262. *Id.* at § 96. An American branch of a foreign bank will play a role similar to that of an American bank in a private placement. *See infra* note 284. A bank in the early stages of a private placement involving debt instruments will advise an issuer on the "appropriate interest rate, maturity, indenture provisions and the timing of the sale." Banks and Securities Law, *supra* note 261, at § 96.01. A bank advising on a private placement of equity securities will have different considerations in formulating its advice. *See* Skigen & Fitzsimmons, *The Impact of the International Banking Act of 1978 on Foreign Banks and Their Domestic and Foreign Affiliates*, 35 Bus. Law 55, 56 (1979) [hereinafter Skigen & Fitzsimmons].

263. *See* Skigen & Fitzsimmons, *supra* note 262, at 56.

264. *Id.*; *see also supra* note 144 and accompanying text. A bank may only purchase securities under Rule 144A for its own account or the account of other qualified buyers, and not for its trust accounts.

As will be discussed in subpart A below, a foreign bank may issue its securities in a private placement with the intention of subsequent resales in the Rule 144A secondary market. It may also act as a purchaser of a foreign private issuer's securities. Finally, it may act as a qualified institutional buyer and purchase securities on the secondary market in reliance on Rule 144A, as discussed in subpart B.

A. Issuance of Securities by a Foreign Bank Under Rule 144A

A foreign bank is eligible to issue its securities in the United States in several ways. The bank may issue securities through its United States branch or agency, or by directly issuing its securities on the United States securities market, either in a private transaction or a public offering.[265] Rule 144A transactions, with respect to the issuance and ultimate resale of foreign bank equity securities in the United States, carry additional restrictions under applicable securities laws which must be met prior to issuance.[266] The most limiting condition for a foreign bank participating in a Rule 144A transaction can be found in the otherwise innocuous definition of a "foreign bank."[267]

For purposes of Rule 144A, a foreign bank that trades its own common stock or other equity security will be deemed an investment company under the Investment Act.[268] Generally, the Investment Act prohibits a foreign bank from offering its unregistered securities to domestic public investors.[269]

However, a private placement of a foreign bank's equity securities is not *per se* prohibited.[270] Section 7(d) of the Investment Act prohibits an unregistered public offering of a foreign bank's securities but does not speak to whether a private offering of a foreign bank's securities is impermissible.[271] This gap in the statutory structure of section 7(d) has led the SEC to rule that the private placement exemption under Rule 506 of Regulation D was applicable to an investment

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265. Zaitzeff, *supra* note 38, at 27. Neither the applicable securities laws nor bank laws prohibit a public offering by a foreign bank of its debt securities or equity securities. *Id.* Foreign banks have issued securities in reliance on an exemption from the Securities Act and Exchange Act. *Id.* at 28.

266. *Id.*; *see also supra* notes 144-145 and accompanying text.

267. *See supra* note 3 and accompanying text.

268. *Id.*

269. A foreign bank will have to seek an exemption from the SEC for the Investment Company Act to issue its equity and debt security. Zaitzeff, *supra* note 38, at 28.

270. *See* 15 U.S.C. §§ 80a-1-80a-64.

271. *Id.* at § 80a-7(a).

company.[272] Accordingly, the exemption permitted a foreign bank to issue its equity security in reliance upon Regulation D without regard for the registration requirements of the Investment Act.

Nevertheless, this freedom to issue securities in reliance on a private placement exemption under the Securities Act was limited in 1984.[273] That year the SEC stated that a non-public offering under section 7(d) must comply with section 3(c)(1) of the Investment Act.[274] Section 3(c)(1) excludes certain issuers from the definition of "investment company" subject to registration under the Investment Act.[275] If a private issuer's outstanding securities are held by 100 or fewer beneficial owners in the United States and the issuer does not make, or presently proposes to make, a public offering of its securities, the issuer does not fall under the definition of an investment company and is not subject to registration.[276] As a result, a foreign bank which has more than 100 beneficial owners residing in the United States must register its securities under applicable law.[277] This burdensome restriction essentially eliminates a foreign bank's ability to privately offer its own securities in the United States domestic market.[278]

In a Rule 144A transaction, foreign banks are generally relegated to participating as qualified institutional buyers.[279] A foreign bank attempting to act as a qualified institutional buyer, however, will face additional regulatory restrictions that limit its business activity in the United States securities markets.[280]

B. The Impact of United States Banking Law on a Foreign Bank's Eligibility as a Qualified Institutional Buyer

A foreign bank wishing to participate in a Rule 144A transaction as a qualified institutional buyer faces additional barriers imposed by

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272. Zaitzeff, *supra* note 38, at 80 (citing Continental Bank, SEC No-action Letter, [1982 transfer Binder] Fed Sec L. Rep. (CCH) ¶ 77,248, at 78,081 (available Sept. 2, 1982)).

273. *Id.* (citing Touche, Remnant & Co. (U.K.) Stein Roe & Farnham, SEC No-Action Letter (available Aug. 27, 1984)).

274. *Id.*

275. 15 U.S.C. § 80a-3(c)(1) (1988).

276. *Id.*; Zaitzeff, *supra* note 38, at 93.

277. 15 U.S.C. §§ 80a-1-80a-3.

278. *See id.* Because the SEC chose to define a foreign bank as a foreign investment bank for purposes of Rule 144A, the likelihood of these banks having fewer than 100 beneficial owners in the United States is remote.

279. *See* Rule 144A, *supra* note 31. Generally, a foreign bank has an opportunity to act as a qualified institutional buyer. It conceivably could act as the seller of securities to such qualified buyers. A foreign bank, however, usually does not participate in this intermediate underwriting role. *See supra* note 262 and accompanying text.

280. *See infra* notes 299-305 and accompanying text.

applicable securities law.[281] In this situation, a foreign bank's business activity may be characterized as an investment in securities traded primarily on PORTAL.[282] Banks, including foreign banks and their affiliates which operate in the United States, are subject to extensive statutory and regulatory control over their lending and other banking activities. Such control may prohibit the investment activities contemplated by Rule 144A.

In 1978, Congress enacted The International Banking Act of 1978 (Banking Act).[283] The effect of this enactment was to place foreign banks on equal footing with domestic banks.[284] Regulation 28.4 under the Banking Act states: "[The] operations of a foreign bank at a Federal branch or agency shall be conducted with the same rights and privileges and shall be subject to the same duties, restrictions, penalties, liabilities, conditions, and limitations that would apply to a national bank at the same location."[285] As a result, a foreign bank operating in the United States would be subject to the Securities Act

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281. *Id.*; *see supra* note 144 and accompanying text.

282. A Rule 144A transaction involves the buying and selling of eligible securities. *See* Rule 144A, *supra* note 31. To date, PORTAL is the most accessible method of effectuating a trade in such eligible securities. *See supra* notes 243-259 and accompanying text.

283. 12 U.S.C. § 3101 (1988).

284. *See* Skigen & Fitzsimmons, *supra* note 262, at 56. Under the Banking Act, the two principal types of banking organizations which a foreign bank may operate in the United States are a branch and an agency, which are offices of the foreign bank and not subsidiaries. These are chartered by the Comptroller of the Currency, an agency of the United States government, so long as the foreign bank engages directly in banking business outside the United States. *Id.*

A federal agency of a foreign bank is an entity that has its place of business in the United States and maintains "credit balances" arising out of the exercise of its banking powers, and may not accept deposits from American citizens. A foreign branch of a foreign bank is an entity that has its place of business in the United States, but which may accept domestic deposits. Generally, in all other respects, the structure and function of an agency and a branch of a foreign bank are indistinguishable. *Id.*

285. 12 C.F.R. § 28.4; 12 U.S.C. § 3101(b) (1988). Generally, a foreign bank which engages directly in a banking business outside the United States may, upon approval by the Comptroller, establish one or more Federal branches. *Id.* at § 3102(a). Such branch is subject to the rules and regulations established by the Comptroller and must conduct its operations "with the same rights and privileges as a national bank at the same location and shall be subject to all the same duties, restrictions, penalties, liabilities, conditions and limitations that would apply under the National Bank Act to a national bank doing business at the same location." *Id.* at § 3102(b). With respect to non-banking activities of foreign banks, "(1) any foreign bank that maintains a branch or agency in a State, (2) any foreign bank or foreign company controlling a foreign bank that controls a commercial lending organization under State law, and (3) any company of which any foreign bank or company referred to in (1) and (2) is a subsidiary shall be subject to the provisions of the Bank Holding Company Act of 1956." *Id.* at § 3106(a). Note, however, that a foreign bank is not permitted to engage in such non-banking activities after December 31, 1985, unless it was lawfully engaged in such activity prior to the enactment of the Banking Act on July 26, 1978.

and the Exchange Act, and, generally, to all other law applicable to a national bank, including the Glass-Steagall Act.[286]

Section 16 of the Banking Act of 1933, known as the Glass-Steagall Act, prohibits banks from engaging in certain underwriting activities and provides that: "the business of dealing in securities and stock by [national banking] associations shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account, and the association shall not underwrite any issue of securities or stock.[287] The Glass-Steagall Act accordingly may restrict a foreign bank from buying securities for its own account and the account of others.[288]

As amended by the Bank Act of 1935, the Glass-Steagall Act

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286. 12 U.S.C. § 227 (1988).

287. *Id.*; *See* BANKS AND SECURITIES LAW, *supra* note 261, at §§ 96.02, 96.05, 96.10, 96.12 (1990). The Glass-Steagall Act focuses on three securities investment activities: (1) bank underwriting of securities; (2) bank purchases of securities; and (3) bank purchases for its own account. *Id.* at § 96.02[2].

288. *Id.* at § 96.10[1]. Alternatively, a foreign bank wishing to serve its customers in a Rule 144A resale transaction could attempt to use a broker-dealer subsidiary. *Id.* Unfortunately, under current law, bank holding companies generally do not have the legal authority to trade in corporate debt or equities. Thus, the foreign bank's eligibility to participate in this market will be limited. Banking Rep. (BNA), vol. 54, No. 23, at 998 (June 11, 1990).

Foreign banks that qualify as "qualified foreign banking organization" (QFBOs) may also acquire an unlimited number of voting or non-voting shares in a foreign company pursuant to § 211.23(f)(5) of Regulation K (QFBO exemption). 12 C.F.R. § 211.23.

Under § 211.23(f)(5), a QFBO may own or control voting shares of a foreign company that is engaged directly or indirectly in non-banking business in the United States, other than that which is incidental to international or foreign business, but subject to the limitations that (a) more than 50% of the foreign company's consolidated assets shall be located, and consolidated revenues derived from outside the United States, (b) the foreign company does not directly underwrite, sell or distribute, nor own or control more than 5% of the voting shares of any company that underwrites, sells or distributes securities in the United States (except under circumstances not relevant here), and (c) if the QFBO holds 25% or more of the foreign company's voting shares, the foreign company (i) must be, or control, an operating company and (ii) the foreign company's United States activities must be the "same kind" of activities as, or related to, the activities engaged in, directly or indirectly, by the foreign company abroad, as determined by the United States census standard industrial classification (SIC) numbers. The foreign company can engage in banking or financial operations in the United States only upon the prior approval of the Board.

A foreign bank should be able easily to determine from its United States regulatory filings whether it is a QFBO. The requirements for qualification include:

(i) A "foreign bank" is an organization that is organized under the laws of a foreign country and that engages in the business of banking.

(ii) A foreign banking organization (FBO) is a foreign bank that operates a branch, agency or commercial lending company subsidiary in the United States, or that controls a bank in the United States, and includes a company of which a foreign bank is a subsidiary.

(iii) A "subsidiary" for purposes of this discussion means any organization 25% or more of whose voting shares are directly or indirectly owned, controlled or held with

permits a national bank, and, therefore, a foreign bank, to purchase for its own account "investment securities" subject to certain maximum holding limitations.[289] Investment securities are defined as any "marketable obligations evidencing indebtedness of any person . . . in the form of bonds, notes and/or debentures."[290]

This exception to section 16 of the Glass-Steagall Act did not affect the otherwise permissible investment in "obligations of the United States," but limited investment to corporate debt securities.[291] Consequently, a bank may not purchase for its own account corporate equity securities. Generally, a bank may only purchase United States government securities and "investment" securities.

This statutory restriction creates two problems for a foreign bank to participate as a qualified institutional buyer in a Rule 144A transaction. First, it restricts the securities a bank may include in meeting the Assets Test. Second, it may restrict a foreign bank from purchasing any type of securities in reliance on Rule 144A, because securities traded in the private placement market are not deemed "marketable" and may not be characterized as investment securities.[292]

Under Rule 144A and the PORTAL rules, a foreign bank must

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power to vote by an FBO or which is otherwise controlled or capable of being controlled by an FBO.

(iv) Generally, an FBO qualifies as a QFBO if, (a) disregarding its United States banking business, more than half of its worldwide business is banking and (b) more than half of its banking business is outside the United States. "Outside the U.S" excludes all assets, revenues or net income, whether held or derived directly or indirectly, of a subsidiary bank, branch, agency, commercial lending company, or other company engaged in the business of banking in the United States.

Furthermore, a QFBO must meet at least two of the following requirements:

(i) Banking assets held outside the United States must exceed total worldwide non-banking assets;

(ii) Revenues derived from the business of banking outside the United States must exceed total revenues derived from its worldwide non-banking business; or

(iii) Net income derived from the business of banking outside the United States must exceed net income from the business of banking in the United States; and must also meet at least two of the following additional requirements:

(i) Banking assets held outside the United States must exceed banking assets held in the United States;

(ii) Revenues derived from the business of banking outside the United States must exceed revenues derived from the business of banking in the United States; or

(iii) Net income derived from the business of banking outside the United States must exceed net income derived from the business of banking in the United States

289. *See* BANKS AND SECURITIES LAW, *supra* note 261, at § 96.02. *Statutes of Variable Rate Demand Notes*, *supra* note 152, at ¶ 85,873. The Banking Act of 1935 is codified in 12 U.S.C. § 228 (1988).

290. *See* BANKS AND SECURITIES LAWS, *supra* note 261, at § 96.02.

291. *Id.*

292. *See infra* note 300 and accompanying text.

meet the Assets Test to be eligible to purchase securities on PORTAL.[293] In calculating the amount of securities owned or invested for its own account pursuant to Rule 144A, a bank may not include United States government securities, bank deposit notes and certificates of deposit, loan participations, repurchase agreements, securities owned but subject to repurchase, or currency, interest rate and commodity swaps, in determining its eligibility.[294] A foreign branch, like its domestic bank counterpart, may be limited by section 16 of the Glass-Steagall Act from holding a predominately high volume of United States government securities.[295] The exclusion of certain types of securities to ascertain the qualifying amount under Rule 144A may block a foreign bank's ability to qualify under the Assets Test. Banks may be placed at a disadvantage compared to other institutions in determining eligibility to qualify as a buyer.[296]

The second limitation confronting foreign banking corporations is the prohibition against investing in securities other than investment securities.[297] An investment security generally refers to a security that, because of its credit rating or credit quality, is deemed to have few speculative credit characteristics.[298] As previously noted, banks,

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293. *See supra* notes 144-145 and accompanying text.

294. Securities Act Release No. 6862, *supra* note 3. Section 2(1) of the Securities Act of 1933 defines the term "security" as follows:

> The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

15 U.S.C. § 77b(1) (1982)

295. Banking Rep. (BNA), vol. 54, No. 23, at 998 (June 11, 1990). A foreign bank may be in a somewhat different position than domestic banks with respect to security holdings if its home country banking laws permit favorable security holdings by the bank. *See id.*

296. *Id.* Rule 144A permits the parent company to aggregate its holdings with its affiliates to determine the qualifying amount, but only if the parent company manages and directs the investments of the affiliate. As a result, both domestic and foreign banks may aggregate their securities holdings with those of a wholly-owned affiliate. Securities Act Release No. 6862, *supra* note 3.

297. Investment securities have been defined, with respect to debt instruments, as an instrument which has a sufficient degree of investment quality. *See Statutes of Variable Rate Demand Notes*, *supra* note 152, at ¶ 85,813.

298. *See Statutes of Variable Rate Demand Notes*, *supra* note 152, at ¶ 85,873.

including foreign banks, are generally prohibited from purchasing any type of security for itself other than debt securities.[299] Notwithstanding this prohibition, the Comptroller of the Currency (Comptroller) has ruled that privately placed securities are not "marketable securities;" thus, they do not qualify as investment securities.[300] Securities traded on PORTAL are restricted securities and would not be considered "marketable securities."[301] As a result, even the purchase of a debt offering under Rule 144A would be impermissible.[302]

Apparently, current banking law, in tandem with Rule 144A, limits a bank's holdings in securities other than debt and United States government securities. Rule 144A sets forth which securities may be used in calculating whether a foreign bank's securities holdings are sufficient to meet the Assets Test. These limits may prevent a foreign bank from being eligible to participate as a qualified institutional buyer.[303] Moreover, should a bank indeed qualify as a buyer, these same restrictions would nonetheless prevent the foreign bank from buying equity stock on PORTAL.[304] Banks and their foreign equivalent will have to wait until the Comptroller or the SEC reconsider their positions.

VI. A Rationale for Change in Banking Law and Rule 144A

A. Should Foreign Banks Be Permitted to Trade in Equity Securities?

The Glass-Steagall Act prohibits trading by a national bank in equity securities.[305] This prohibition dates back to the 1930s and was

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299. *Id.*; Banks are permitted to purchase equity securities subject to certain value limitations tied into the amount of capital assets the bank owns. *See supra* note 285, app. V-1, (citing Comptroller investment regulations). For example, one type of security a bank may invest in is a "Type III" security. Its holding of such equity securities, however, may not exceed 5% of the bank's capital and surplus.

300. *See supra* note 297 and accompanying text. Marketable has been defined as a security that can be sold with a "predictable immediacy . . . quickly sold at a value approximating its worth." *Id.* In addition, securities not registered under the federal securities laws and unable for public sale in the United States are considered to be less marketable. *See* Fed. Banking L. Rep. (CCH) ¶ 85,888 (Jan. 1987). As a result, the Comptroller has traditionally viewed marketable securities not to include private placement securities. Fed. Banking L. Rep. (CCH) ¶ 85,898 (Feb. 1989).

301. A security traded in reliance on Rule 144A must have originally been offered through a private placement. *See* Securities Act Release No. 6862, *supra* note 3.

302. *Id.*

303. *See supra* notes 281-304 and accompanying text.

304. *Id.*

305. 12 U.S.C. § 24. Many scholars and Congress have advocated the repeal, replace-

born out of the stock market crash of 1929.[306] The passage of the Act reflected the Congressional answer to the excessive investment activity by large institutional banks participating in the stock market prior to the crash.[307] Congress presumed that excessive investment in the securities market contributed to the crash.[308] Furthermore, many thought that the collapse of the stock market and resulting depression were, in part, directly attributable to the reckless investment in high risk securities by large financial institutions.[309] In fact, such institution's capital assets were heavily invested in equity securities.[310] Unlike contemporary securities legislation, the law in 1929 neither adequately regulated the market nor protected an investor's ability to make an informed purchase through the enforcement of information disclosure laws, liability provisions or anti-fraud provisions.[311]

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ment or amendment of the Glass-Steagall Act. *See* Note, *An Alternative to Throwing Stones: A Proposal for the Reform of Glass-Steagall*, 52 BROOKLYN L. REV. 281 (1986) [hereinafter Note, *An Alternative*]; Isaac and Fien, *Facing the Future - Life Without Glass-Steagall*, 37 CATH. U.L. REV. 279 (1985) [hereinafter Isacc and Fein]; Note, *After Natwest: Are Camp "Subtle Hazards" and "Union of Powers" Analysis Dead?*, 37 CATH. U.L. REV. 791 (1985); Note, *The D.C. Circuit Affirms Further Bank Expansion into Securities Business*, 56 GEO. WASH. L. REV. 736 (1988); Note, *Bankers Trust II: Underwriting Commercial Paper Placement and the Risk of Loss Under the Glass-Steagall Net*, 76 KY. L.J. 497 (1987). This article does not necessarily proffer that the Glass-Steagall Act should be repealed, but rather, briefly reviews the Act, its history and purpose in relation to today's regulated securities market and suggests that its prohibition on bank trading under Rule 144A securities should be reexamined.

306. *See* BANKS AND SECURITIES LAW, *supra* note 261, at § 96.02.

307. *Id.* Prior to 1933, commercial banks, primarily through affiliates had become dominant market players in investment securities. *See id.* at 96-5. In 1891, the United States Supreme Court ruled that National Banks were prohibited from trading in securities and, in response, such financial institutions organized securities affiliates to operate securities activities. *See id.* at 96-6. Earlier prohibitions on investment activity, however, began to erode, culminating in 1927 with the enactment of legislation permitting bank investment in marketable debt instruments. *See* BANKS AND SECURITIES LAW, *supra* note 261, at 96-7. After the collapse of the stock market in 1929, Congress reexamined the liberalization of statutory and regulatory contracts over such banking institutions and their investment activities and discovered "questionable and unsound practices that threatened the safety of bank depositors' funds, the reputation of the nation's banks, and the financial strength of banks." *Id.* at 96-8.

308. *Id.* Three of the nation's largest commercial banks had become heavily invested in securities of doubtful value. *Id.* The enactment of the Glass-Steagall Act was an attempt to tighten regulatory control over the banking industry in reaction to the depression years. J. WHITE, BANKING LAW 33 (1976) [hereinafter BANKING LAW].

309. *See* BANKS AND SECURITIES LAW, *supra* note 261, at § 96.01; Note, *An Alternative*, *supra* note 305, at 282.

310. *See* BANKS AND SECURITIES LAW, *supra* note 261, at § 96.01.

311. The Securities Act and Exchange Act had yet to be enacted. Their enactment was an attempt to react to and control the harmful securities trading activity that may have helped precipitate the collapse of the national economy in 1929. *See id.* at 204; *See* §§ 11, 12 and 17 of the Securities Act (1988) for liability based on material misstatements or omissions or fraud under the securities laws. 15 U.S.C. § 77(k)(1)(q); *see also* Zaitzeff, *supra* note 38, at 19. The

With no legal structure in place to control certain investment activity, in several notable instances, large financial institutions invested in undercapitalized companies or in companies undertaking risky business endeavors. These latter enterprises held securities which often had no value other than some fictitious value created by the market or perpetrated through fraudulent trading activity.[312] Some suggested that as these companies began to collapse financially, large financial institutions were unable to recoup their capital investment and, having overextended themselves in the securities market, few assets remained with which to cover liabilities (i.e., depositors' accounts).[313] What emerged after the collapse of the stock market was a regulated industry limited to investment in debt instruments, that is, limited essentially to the purchase of high yield assets.[314]

Whether commercial bank failures in the 1930s may be attributed to investment in securities is debatable.[315] The excessive risk often associated with securities investments by banks and the need to

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Exchange Act's principal purpose is to promote trading in the domestic resale market by requiring full disclosure and imposing liability on persons perpetrating fraudulent transactions. *See generally* 15 U.S.C. § 77. Generally, any securities offered or sold by means of interstate commerce or the United States mails pursuant to § 5 of the Securities Act must be registered under the Securities Act. 15 U.S.C. § 77(c) (1988).

312. BANKS AND SECURITIES LAW, *supra* note 261, at § 96.02. For example, National City Bank had written off a $25,000,000 loan to Cuban Sugar Companies and recovered the loss by organizing a dummy corporation that bought the loans. The purchase was financed by the sale of the dummy corporation's stock held by its holding company to bank shareholders. *Id.*; *see also* Note, *An Alternative*, *supra* note 305, at 281. Other abusive practices by commercial banks in the securities market disclosed by Congress included:

1. Banks establishing subsidiaries or departments whose profit margin was tied to the volume sales in securities;
2. Banks transferring poor quality bonds to trust accounts and correspondent banks which did not have matching assets to cover such liabilities;
3. Banks encouraging churning on the sale and purchase of underwritten securities to capture the high profits paid by corporations to undertake such underwriting risk; and
4. Banks using investment banking affiliates "to support the price of a bank's own stock by purchasing that stock." *See* BANKS AND SECURITIES LAW, *supra* note 261, at § 96.02.

313. *See* BANKS AND SECURITIES LAW, *supra* note 261, at § 96.02. It was believed that "banks had diverted their deposits to finance unsound investments, which threatened the safety of their depositors' funds." *Id.*

314. *See* Note, *An Alternative*, *supra* note 305, at 281. "[T]he essential accomplishment of the new legislation is that it makes it possible for banks more readily to convert their assets into cash than was the case before." BANKING LAW, *supra* note 308, at 33 (quoting President Roosevelt in a radio transmission delivered from the President's study on March 12, 1933). The enactment of the Glass-Steagall Act was an attempt to separate security investment activities from traditional banking activities. *Id.* at 34. The Act forbids national banks from using the Federal Reserve for speculative purposes, including investment trading in securities. *Id.*

315. *See* Garten, *supra* note 77, at 512.

prohibit such investment, may be non-existent in today's regulated securities market, especially within Rule 144A transactions.[316] Furthermore, restricting a bank's activities to lending-based activities does not lessen the risk of bank failure nor protect a depositor's funds.[317] The risk associated with current lending activities that may encourage the largest domestic banks to write off billions of dollars in loans to third world countries[318] is perhaps no greater than that associated with amending Glass-Steagall to permit bank trading in equity securities on PORTAL. Because of present day regulation of the banking industry which limited banks' business activities to traditional practices of lending, the Glass-Steagall Act's prohibition on trading in equity securities has eroded.[319] Indeed, the Federal Reserve Board has effectively acknowledged this change by steadily permitting banks to engage in traditionally prohibited securities trading activity under Glass-Steagall.[320]

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316. *Id.* at 528.

317. Id.; *see also* Isaac and Fien, *supra* note 305, at 528.

318. *See* Garten, *supra* note 77, at 528; *See* TIME, Aug. 6, 1990, at 30; BUSINESS WEEK, Aug. 13, 1990, at 98. "Diversification [into trading in securities] may itself be in the best way to limit risk." Garten, *supra* note 77, at 545.

319. Garten, *supra* note 77, at 512. In December, 1989, the Security Industry Association proposed a plan to amend Glass-Steagall to allow bank holding companies to own full service security companies as subsidiaries. *See* Fein, *Securities Activities of Banks and Their Affiliates: Significant Developments in 1989-1990*, in SECURITIES REGULATION OF BANKS AND THRIFTS IN THE 1990'S 33 (Practising Law Institute Handbook No. 688 (1990)) [hereinafter Fein].

> On January 4, 1990, the Board approved applications by [a foreign bank] to engage in securities underwriting and dealing activities through § 20 subsidiaries. The Board denied the applicants' request that overseas operations of foreign banks generally be exempt from the firewalls. The Board did make an important concession to the structural requirements of the foreign banks, however, by permitting the parent foreign banks to directly own and fund their § 20 subsidiaries. Minor adjustments to the firewalls also were approved. The Board permitted one management interlock between an American branch of a foreign bank and its § 20 affiliate as a means of providing the foreign bank with a mechanism to monitor the § 20 affiliates's operations. In contrast, domestic bank holding companies are allowed no interlock between a § 20 subsidiary and affiliated banks. The Board also permitted foreign-owned as well as domestic § 20 subsidiaries to purchase and sell ineligible securities with affiliates that are participating in simultaneous underwritings in more than one national market during the underwriting period.

Id. Presumably, foreign banks should not be regulated to the same extent, nor should they be prohibited from trading in equity securities because they are not investing domestic depositor's funds to the same extent as domestic banks. Nor do they affect American financial security to the same extent.

320. Fein, *supra* note 319, at 33. In a letter to the Federal Reserve Bank of New York, the Board of Governors of the Federal Reserve System stated that they would review policies associated with further expansion of bank holding companies trading in equity securities. *Id.* BRENTON AND DOUGLAS, FEDERAL BANKING LAWS 1-9 (1987 ed.) [hereinafter BRENTON AND DOUGLAS]. Within the Department of Treasury, the Comptroller of the Currency is charged with executing banking/monetary laws passed by Congress; the Comptroller is under

In September 1990, the Board took the unprecedented step of approving of a bank holding company's application to trade in corporate securities, thereby significantly curtailing banking regulations that previously separated banking and securities investment activities.[321] This remarkable ruling is limited, however, by several restrictions. One limitation prohibits banks from using government-insured deposits to finance investment activities.[322] This prohibition protects depositors' funds. In addition, only a separate affiliate of a bank, with its separate capital and management, may actually effect securities transactions as permitted by the ruling. The affiliate's revenues in the form of stocks and bonds, may not exceed ten percent of its total revenues.[323]

Nevertheless, the erosion of Glass-Steagall has occurred where the formally prohibited activity could be shown not to: (i) jeopardize depositors' funds, (ii) create financial instability within a bank, (iii) create a conflict of interest that might impair a bank's giving disinterested investment advice, (iv) permit transfer of valueless securities to a bank's trust account or (v) exploit confidential information in the securities market of information received in its commercial banking practice.[324] For example, the Federal Reserve Board has determined that certain investment activities in the securities market do not constitute underwriting or dealings in securities banned by the Glass-Steagall Act including, assisting in a private placement of securities and in underwriting general obligation bonds.[325]

In 1977, the Federal Reserve Board concluded that a bank's negotiation and participation in the placement of an issuer's securities and solicitation of investors for a contingent fee in a private placement transaction did not constitute an underwriting,[326] even though such activity clearly constitutes an underwriting under the Securities Act. The Board reasoned that such activity was not equivalent to purchasing the issuer's securities for resale, notwithstanding applicable securi-

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the supervision of the Board of Governors of the Federal Reserve Systems. *Id.* (citing 12 U.S.C. § 1) (1988). The Board of Governors is composed of seven members, appointed by the President of the United States. 12 U.S.C. § 241 (1988). The Board has the authority to examine the accounts and affairs of banks and delegate such responsibility accordingly. *See id.* at § 248.

321. N.Y. Times, Sept. 21, 1990, at D1, col. 1.

322. *Id.*

323. *Id.* "To bypass the restrictions of the Glass-Steagall Act, the Federal Reserve used a loophole in the law that allows a bank holding company to have a securities unit so long as that unit is not 'principally engaged' in securities activities forbidden by Glass-Steagall." *Id.*

324. *See* BANKS AND SECURITIES LAW, *supra* note 261.

325. *See* Garten, *supra* note 77, at 528-30.

326. *See* BANKS AND SECURITIES LAW, *supra* note 261, at § 96.10[1].

ties laws.[327] The Board based its decision on: (i) other banking regulatory procedures which enabled bank regulators to monitor and examine banks participating in such activity on a continuing basis; this enables regulators to uncover any conflict of interest in the bank's role as both advisor and underwriter, (ii) the fact that no banking funds were directly used in the transaction; therefore, depositors' funds were not at risk, and (iii) investors did not rely on the bank for advice but relied on the information publicly available and disclosed under the Securities Act.[328]

Similarly, the Comptroller has ruled that banks may underwrite general obligation bonds backed by the issuer's full faith and credit.[329] This privilege is expressly permitted pursuant to the general obligations exception of the Glass-Steagall Act.[330] Municipal securities, generally, are bonds supported directly or indirectly by the credit of the State or locality possessing general powers of taxation.[331] Since these bonds are secured by a governmental entity, the risk associated with investing in securities is sufficiently reduced to permit investment activity without jeopardizing a financial institution's economic stability or risking depositors' funds.[332] This doctrine, however, has been expanded and may include, for example, trading by a bank in governmental agency bonds secured by state lease obligations.[333] This shift to deregulation and diversification of banking activities to include investment is not wholly attributable to a change in circumstances. This shift is a result of reevaluation of banking regulatory philosophy.[334] The justification for restricting a bank from active trading in equity securities such as Rule 144A transactions was the belief that lending-based activities were safer because they placed a depositor's funds at lesser risk than investment in equity securities.[335]

The traditional lending philosophy emerged out of the regulatory enactments of 1930.[336] It consisted of deposit-taking and lending activities designed to reduce the risk of bank failure and to protect as-

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327. *Id.* The Board of Governors of the Federal Reserve System (Board) oversee member banks while the Comptroller is responsible for the regulation of national banks.

328. *See id.*

329. *See* BANKS AND SECURITIES LAW, *supra* note 261, at § 96.10[1].

330. *Id.*

331. *Id.*

332. *Id.*

333. *See* BANKS AND SECURITIES LAW, *supra* note 261.

334. *See* Garten, *supra* note 77, at 507.

335. *Id.*; Note, *An Alternative*, *supra* 305, at 290.

336. *See* Note, *An Alternative*, *supra* note 305, at 290; Garten, *supra* note 77, at 507-25.

sets.[337] In this model, current lending activities are restricted to deposit-taking and commercial loans. Though somewhat simplistic, this model is useful in examining bank securities investment and lending activities.[338] For example, banks could not exceed caps on the interest rates earned on a depositor's account.[339] Generally, the rate of interest on any money lent to a borrower reflected the rate earned by depositors on their bank accounts.[340] By placing a cap on the rate of interest which a depositor's account may earn, the Federal Reserve Board effectively eliminated a bank's inclination to make high-risk, high-yield loans to cover expenses associated with depositors' accounts.[341]

The investment decision risk assumed by a bank under this model is not removed or significantly reduced by such regulation.[342] A bank officer must still evaluate the risk associated with providing bank funds to a particular borrower and analyze the sufficiency of the security covering its loan.[343]

In addition, this model is regulated through government agencies designed to monitor compliance, in contrast to the administration of applicable securities laws based on enforcement and imposition of penalties.[344] The administration of banking regulation is designed to detect and correct potential problems or existing problems that threaten an institution's financial integrity.[345] Nevertheless, the monitoring of financial institutions has not prevented the collapse of many institutions, either for political or administrative reasons.[346] Nor can such regulators be expected to effectively monitor the voluminous daily loan transactions or deposit transactions undertaken by banks,[347] or to have the sophistication to evaluate the risk attached to a particular loan transaction.[348] Banks have the burden of evaluating such risks.[349] The risk will be borne by the bank's depositors.[350]

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337. Garten, *supra* note 77, at 507-25.

338. *See id.*

339. *Id.*

340. Garten, *supra* note 77, at 507-25.

341. *Id.*

342. *Id.*

343. *Id.*

344. Garten, *supra* note 77, at 507-25. As a condition of membership in the Federal Reserve System, member banks are subject to examination by examiners as directed by the Board. 12 U.S.C. § 325 (1988).

345. Garten, *supra* note 77, at 507-25.

346. *See* N.Y. Times, Sept. 22, 1990, at 33.

347. *See* Garten, *supra* note 77, at 520.

348. *Id.*

349. *Id.*

In addition, many bank lending activities have declined in profitability as competition from outside the banking industry has captured a portion of the industry's market.[351] Internal competition has also reduced profitability as banks must work harder to attract clientele.[352] This decline in profitability may threaten a bank's financial stability.[353] An unprofitable industry leads to financial instability and jeopardizes the financial institution's economic integrity which Glass-Steagall was designed to prevent.[354] Consequently, the traditional regulatory approach to insure financial integrity may not function as admirably as expected.[355]

The risk associated in amending Glass-Steagall to permit trading by banks in equity securities on PORTAL may be comparable to the economic risk of maintaining current lending activities.[356] The evaluation of risk remains the same.[357] A bank should evaluate the risk based on available information to determine whether the investment is likely to be profitable.[358]

In a Rule 144A transaction, a foreign bank's investment in equity securities will fall within the objectives of the Glass-Steagall Act.[359]

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350. *Id.*

351. *See* Garten, *supra* note 77, at 520. *See also* Isaac and Fien, *supra* note 305, at 202. "[T]he profit and assets quality of commercial banks have declined and their viability as the bulwarks of the nations's financial and monetary system is in question." *Id.* An example of encroachment on financial activities usually reserved for banks is the recent federal court ruling allowing Sears, Roebuck & Company to issue visa cards. N.Y. Times, Feb. 26, 1991, at D1. Since outsiders have encroached on the banking industry, banks argue they should be permitted to encroach upon the business of other industries.

352. *See* Note, *An Alternative*, *supra* note 305, at 204 n.15.

353. Isaac and Fein, *supra* note 305, at 282; Garten, *supra* note 77, at 525.

354. *Id.*

355. *Id.*

356. A greater question: why subject foreign banks to the jurisdiction of United States banking laws with respect to certain securities trading activities if they have few domestic depositors and their failure does not directly jeopardize American interests? This article leaves that discussion for another day. In fact, foreign banks are regulated to a lesser degree than their American counterparts. *See supra* note 319 and accompanying text.

357. Bank officers must evaluate the risk in providing loans and, similarly, may evaluate the risk in investing in a company's securities based on available corporate and financial data. Substantively, a bank analyzes the sufficiency of collateral prior to agreeing to advance a loan and analyzes corporate and financial data as it might prior to investing in a speculative securities investment. The risk analysis is fundamentally the same (i.e., based on currently available information is investment by the bank in a company secure enough to provide the bank with an adequate return on its investment). Furthermore, the share value of a security traded in a Rule 144A transaction may reflect its fair value. *See* Banking Rep. (BNA), vol. 54, No. 23, at 998 (June 11, 1990). Its speculative characterization may be inappropriate.

358. *Id.*; *See* Garten, *supra* note 77, at 543-47.

359. Glass-Steagall was enacted to prevent certain abuses by banking entities in securities investment. *See* Note, *An Alternative*, *supra* note 305, at 282. The regulatory structure of the

Furthermore, the risk often associated with investing in equity securities may be reduced in a Rule 144A transaction.[360] Unlike a debt instrument, the value of the security will be subject to market forces.[361] However, in a closed secondary market limited to trading amongst certain qualified institutional buyers that have the requisite sophistication to value securities, the fair value will likely be reflected in its quoted value.[362] The value of a security, like the security attached to a debt instrument, may decline. Given the nature in which a Rule 144A security is traded, the risk that a securities quotation on

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Securities Act and the Exchange Act and their anti-fraud and liability provisions will control and make bank activities accountable in conjunction with the closed market structure created by Rule 144A and PORTAL. *See generally* 15 U.S.C. § 17 (1988).

360. *See* Note, *An Alternative*, *supra* note 305, at 282. Securities traded on PORTAL pursuant to Rule 144A are expected to be high yield, high quality debt instruments and secure equity investments are expected to sell "with reasonable promptness at a price which corresponds with its fair value". Banking Rep. (BNA), vol. 54, No. 23, at 948 (June 11, 1990). Accordingly, the speculative nature of a securities investment is reduced. Evaluation of the risk, however, always remains with the investor.

361. *See* Garten, *supra* note 77, at 542.

362. *See* Rothwell, *supra* note 144, at 189. Theories for the valuation of the intrinsic value of a share abound. *See generally* Banks & Carnes, *Share Valuation - A Chance for Financial Literacy*, 23 CAL. W.L. REV. 192 (1987). For example, it has been suggested that Delaware courts hold that the value of a share should be based on the "amount . . . which would be produced by an arm's length negotiation" by its sale. *Id.* at 202. This reflects a share's market price. Another theory is based on an efficient market hypothesis. *See* Note, *"Fair Value" Determination in Corporate "Freeze-outs", and in Security and Exchange Act Suits: Weinberger, Other, and Better Methods.*, 19 VAL. U.L. REV. 521, 555 (1985). Under this theory, the market price reflects a shares real value based on past events and information currently available. *Id.* Under this theory several assumptions are made so the market value equals the shares real value, including: (i) market participants are rational profit maximizers, (ii) market participants are numerous, (iii) market participants have near perfect knowledge, and (iv) market competition will affect the intrinsic value of the shares and cause new information to be made public. *Id.* at 557.

In essence, the Rule 144A market creates all four assumptions. The Rule is based on the notion that qualified institutional buyers can fend for themselves. Securities Act Release No. 6862, *supra* note 3. Such buyers have the sophistication and experience to purchase Rule 144A securities. *Id.* Thus qualified buyers may be deemed rational profit maximizers. Moreover, Rule 144A provides for disclosure of information by non-reporting issuers. *Id.* Qualified buyers may have the leverage to exert additional information from issuers or about issuers in connection with a 144A offering. The information usually disclosed in a private placement is equivalent to or exceeds that required under United States securities laws. Panel Discussion, *supra* note 20. Thus, current information is made available and qualified buyers have the knowledge to invest wisely.

No cap on the number of market participants exists. *See* Rule 144A, *supra* note 31. Qualified buyers may resell their eligible securities to any number of other qualified buyers. *Id.* In addition, PORTAL facilitates the impact any favorable or unfavorable information would have on the value of a share by instantaneously changing a shares quoted price in response to the release of such information. Thus, the secondary market created by Rule 144A is a closed system of sophisticated buyers. *Id.*; H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 6-6. In such a trading environment the market price is likely to represent the share's intrinsic value.

PORTAL does not reflect its real value may be reduced.[363]

Moreover, applicable securities laws and bank regulations will assure the Federal Reserve Board that the foreign bank is knowledgeable about its investment in an issuer.[364] As a result, the financial stability of a foreign bank sophisticated in securities investment will not be threatened by prudent investments in such securities. For example, the SEC chose to employ a second condition of eligibility to banking corporations participating as qualified institutional buyers through application of the Net Worth Test. The SEC found, unlike other institutions, domestic banks and savings and loan associations deposits are federally insured. These institutions may purchase securities using public funds without placing themselves at the same risk as other institutions.[365] Consequently, the SEC reasoned the amount of securities owned under the Assets Test (the first condition of eligibility) is not, on its own, sufficient to determine size and investment sophistication for purposes of the Rule.[366] The Assets Test, therefore, is used in conjunction with the Net Worth Test to better measure the sophistication of the respective institution.[367] To avoid placing domestic banks at a competitive disadvantage, the SEC ruled that foreign banks, or their equivalent, as well as their United States branches, are also subject to the Net Worth Test.[368]

In addition, certain capital investment limitations could be expanded.[369] Currently, a national bank may invest in certain types of

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363. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at § 6.06.

364. Both the Securities Act and Exchange Act regulate trading in securities; the Comptroller regulates national banks. The dual application of securities law and bank laws that provide for monitoring and penalties for misconduct should suffice to control harmful activity if foreign banks are permitted to trade on PORTAL.

365. Securities Act Release No. 6862, *supra* note 3.

366. *Id.*

367. *Id.*

368. *Id.* Additional protective measures exist. For instance, if public interest and investor protection require, the SEC may suspend trading in any security for 10 days.

369. Permissible trading in securities by foreign banks does not have to include complete removal of limitations that restrict the amount of securities a bank may hold for its own account. *See* Isaac and Fein, *supra* note 305, at 284. There should be no "carte blanche" for banks to enter the securities market. *Id.*; *see also* Karmel, *New Rules for Trading Foreign Securities*, N.Y.L.J., Oct. 18, 1990, at 3, col. 1. Roberta Karmel, former commissioner of the SEC, commented on the Federal Reserve Boards grant of power to J.P. Morgan & Co. to underwrite equity, stating that it was tantamount to removing "the wall separating commercial and investment banking." Ms. Karmel noted that banking agencies are not expert in regulating security activities, nor has the SEC had experience in regulating banking activities. As a result, banks entering the securities market will need to be regulated if continued deregulation under the Glass-Steagall Act occurs. *Id.* The SEC's ability to extend jurisdiction over the banking industry may be limited and thus new regulations may have to be formulated. Ms. Karmel noted that Congress is likely to favor functional regulation but pointed out that "a

securities for its own account not to exceed a certain percentage of its capital reserves.[370] This limit is intended to reduce the risk of a bank overextending its funds in a securities investment.[371]

One final point worth noting is that foreign bank's investment interests and those of current investors will not conflict as competing purchasers.[372] The market is restricted to investment among qualified buyers.[373] Most clients advised by foreign banks will not participate in a Rule 144A transaction; the client will not be an institution with the requisite sophistication.[374] Furthermore, any other potential indirect conflict can be lessened by having the commercial and investment operations of a bank sufficiently isolated. This would remove such conflicts of interest between a foreign bank as underwriter and investment advisor. Confidentiality of information acquired by a bank through its commercial practice can be prevented from reaching its investments division.[375] For example, English investment houses carry on both the function of underwriter and advisor, provided a "chinese wall" exists between the divisions that carry on these functions sufficient to prevent any cross exchange of information.[376]

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paramount current problem is establishing appropriate capital adequacy standards. The problems with existing capital adequacy regulation can be seen . . . in the failure of federal banking agencies to predict and prevent massive bank failures." *Id.* at 7. Ms. Karmel also expressed concern on whether the Federal Deposit Insurance Corporation can adequately provide protection to banks entering the securities field, as well as the failure of bank regulators to anticipate and solve bank industry woes. Consequently, one solution may be a Congressionally enacted regulatory structure whereby bank holding companies must separate into subsidiaries for securities, banking, commodities and insurance activities. This would enable each subsidiary to be regulated by different federal agencies. *Id.*

370. Fein, *supra* note 319, at 39-40. With respect to bank holding companies, the Federal Reserve Board has increased the percentage to 5-10% of the total revenues the bank holding company's subsidiary may trade in ineligible securities (i.e., equity stock).

371. *Id.*

372. *See* Rule 144A, *supra* note 31. A foreign bank must have a sizable securities portfolio to demonstrate its sophistication to qualify to buy eligible securities under Rule 144A. Presumably, a bank's client would not be as sophisticated under Rule 144A and, therefore, ineligible to participate as a buyer.

373. *Id.*

374. *Id.*

375. O.C.C. Notice 90-3, *reprinted in* SECURITIES REGULATION OF BANKS AND THRIFTS IN THE 1990'S 645, 657 (Practising Law Institute Handbook No. 688 (1990)) [hereinafter O.C.C. Notice]. In the 1980s, Congress in fact proposed several bills that would have amended the Glass-Steagall Act and called for the institution of "firewalls" between a bank and its securities affiliate; the affiliate being a broker-dealer registered with the SEC and permitted to engage in a full range of securities activities. *Id.*

376. H. BLOOMENTHAL, SECURITIES LAW HANDBOOK 927 (1989-1990). "London is unique among the three financial centers of the world (including New York & Tokyo) in that it is the only one that does not require a separation of investment and commercial banking." *Id.* As a general overview of Britain's securities regulation, on April 29, 1988, Britain initiated an authorization day which permitted only authorized persons to engage in the investment busi-

B. Expand the Definition of "Marketable Security"

A security is marketable if "it may be sold with reasonable promptness at a price which corresponds reasonably to its fair value."[377] Originally, the Comptroller ruled that securities issued through a private placement were not marketable because, in part, the distribution of securities of an issuer under appropriate exemptions, in particular the section 4(2) exemption and Regulation D exemptions, only permitted an issuer to distribute its securities to a limited number of qualified investors subject to remarketing restrictions.[378] Upon purchase, such securities were restricted and generally could not be resold.[379]

Other factors contributing to the characterization of private placement securities as "unmarketable" was the type of issuer, buyer and security purchased in this market.[380] As discussed in Part I, the

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ness as restructured by the International Stock Exchange (ISE) and the Financial Services Act of 1986 (FSA). Authorized persons consisted of new member merchant banks and foreign banks. Restrictions on dual capacity and floor trading by a limited number of persons were eliminated, and, in its place, a NASDAQ type automated quotation system was installed. *Id.* at 928-29. The FSA created a multi-tiered system of securities regulation. The lowest tier is composed of self-regulating organizations (SROs) that make and enforce rules amongst their fellow members in the financial industry. *Id.* The highest tier entity is the Department of Trade and Industry which delegated much of its authority, however, to the Securities and Investment Board (SIB), a private sector agency. The SIB regulates the SROs, Recognized Investment Exchanges, Recognized Professional Bodies (RPBs), and other authorized non-SRO-RPB members. Only a recognized member of an SRO, RPB or other authorized person, or another European Community state, or exempt entity may engage in any investment activity. *Id.*

SROs regulate the business activities of companies carrying on investment activities. They monitor and enforce compliance with its rules and the FSA. The Securities Association is the SRO for most members of the ISE and is the largest in terms of investment business, which includes 200 branches of foreign banks. *Id.*

In comparison, NASD and the national exchanges in the United States are self-regulating organizations. American SROs provide rules and regulations for participating members which include, *inter alia*, material disclosure in a sufficient manner. The FSA, however, does not create an SEC-type organization, yet many SEC structures were incorporated into the Securities Association Rule Book. For example, incorporation of such SEC-type policies include, among others, the requirement that employees of a firm must disclose to any customer investing in securities any material interest the firm or a person connected therewith has in a transaction or investment. Generally, receipt of a commission with respect to an offering may be by prospectus if a customer receives a prospectus prior to the transaction and such prospectus discloses the firms interest. H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41, at 33. There is a general duty to disclose information regarding assets, liabilities, financial position, profits and losses, and prospects. Note, *International Trade Regulation of London Financial Markets*, 28 HARV. INT'L L.J. 696, 200 (1987).

377. *See Statutes of Variable Rate Demand Notes*, *supra* note 152.

378. Fed. Bank L. Rep. (CCH) ¶ 85,898 (Feb. 1985).

379. *See supra* note 92 and accompanying text.

380. *See* Fed. Banking L. Rep. (CCH) ¶ 85,634. Such factors as the size of the offering,

private placement market developed in response to institutional needs resulting in trading securities as assets, rather than investments, amongst a small number of purchasers.[381] Consequently, no active trading occurred in these types of instruments; the market was essentially illiquid and the securities issued in a private placement were characterized as "unmarketable."[382]

The advent of PORTAL and the implementation of Rule 144A, with its stated objective of creating a more liquid secondary market, put the mechanisms in place to build a private placement market sufficiently active to satisfy the Comptroller's marketability test. This new market is still in developmental stages but its more valuable use could be in the trading of equity securities.[383] Currently, the private placement market is superbly adapted to facilitate periodic trading in complex debt securities. This existing market will likely continue.[384] An active secondary market, with trading in restricted equity securities and certain other debt instruments, will be revolutionary. Rule 144A essentially eliminates a primary reason for characterizing a privately placed security as unmarketable by removing the limitation on resale of these securities.

Under Rule 144A, the number of qualified buyers of securities in reliance on the safe-harbor is unlimited.[385] These buyers may sell any number of such securities to an unlimited number of other qualified buyers.[386] In addition, securities traded on PORTAL are essentially new issues to the quasi-public market of PORTAL.[387] There are no restrictions on the quantity of securities placed in this market.[388] Nor are there any limitations on the number of securities resold to qualified investors.[389] PORTAL, like NASDAQ, allows instant access to a securities board with relevant information, enabling quotes and bids to be quickly obtained. Furthermore, PORTAL's international appli-

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the anticipated number of purchasers, the development of a secondary institutional market and the collateralization (for debt instruments) will be considered in determining a security's marketability. *Id.*

381. *See supra* notes 19-20 and accompanying text.

382. *See id.*; *see generally supra* notes 379-380 and accompanying text.

383. *See supra* notes 239-255 and accompanying text.

384. *See supra* note 20 and accompanying text.

385. *See* Rule 144A, *supra* note 31. Such sellers and qualified institutional buyers will have no prior business relationship. *See* Quinn, *supra* note 14, at 90.

386. *See* Rule 144A, *supra* note 31.

387. *See supra* notes 238-255 and accompanying text.

388. *Id.*

389. *Id.*; Securities Act Release 6863, *supra* note 6. Regulation S will also provide mobility and access to trading world-wide. *Id.* Such access should enhance the marketability of the security.

cation and settlement procedures promote trading in eligible securities. These conditions demonstrate that a privately placed security traded on PORTAL will be "marketable."

These conditions (including PORTAL's ability to facilitate trade and the unlimited numbers of securities trading amongst large numbers of investors) are different than the traditional private placement consisting of the purchase of an instrument as an asset and the sale occurring in an established relationship between the issuer and buyer.[390] Indeed, the conditions that led to privately-placed securities being described as unmarketable have changed.[391] To a great extent, some of the original factors that helped shape the type of securities traded in the secondary market no longer exist, such as the modified holding period of Rule 144.[392] The new securities regulations are designed to create a liquid market which will shape a new type of investment security that can be "quickly sold at a value approximating its cost."[393] Clearly, the securities laws and market players of the past fifty years that created an "unmarketable" private placement securities, have evolved. This evolution will continue and Rule 144A should contribute to a change in this characterization.

VII. Structuring an Offering for Resale on the Secondary Market

Accordingly, the market created by Rule 144A and Regulation S will require a different approach in offering securities. Arguably, the secondary market created by Rule 144A and applicable securities and banking laws is sufficient to permit securities trading by foreign banks and to preserve the purpose of Glass-Steagall. Further safeguards, such as restrictive covenants on the resale of a Rule 144A security and disclosure of pertinent information, may be built into the transaction to reduce the risk associated with participation in a Rule 144A transaction.

As a result of Rule 144A and Regulation S, a foreign private issuer will be able to construct unique offerings. A two-tranche offer-

390. Panel Discussion, *supra* note 20.

391. *Id.* In fact, the SEC changed its position that restricted securities are generally illiquid with respect to the purchase of securities by open-ended investment companies and ruled that liquidity of Rule 144A securities would now be a question of fact. *See* Quinn, *supra* note 14, at 78. The factors the SEC uses to evaluate liquidity also could be used by the Comptroller. These factors include: (i) the frequency of trades and quotes for the security; (ii) the number of purchasers of the security; (iii) dealer undertakings to make a market in the security; and (iv) the nature of the security and marketplace trades. *Id.* at 79.

392. Panel Discussion, *supra* note 20.

393. *Id.*; *see supra* notes 377-392 and accompanying text.

ing is one example. Keeping within the parameters of Regulation S, an issuer may offer one tranche of its securities publicly, according to its applicable home country securities laws, and the other tranche to United States nationals pursuant to a private placement for subsequent resale on PORTAL.[394]

A. Initial Structure

Two tranche securities will be offered in two nation's securities markets subject to two sets of securities laws.[395] This two-market approach will require changes in the foreign private issuer's offering documents. The initial structure should reflect the laws of the issuer's home country. For example, French corporate law contains several provisions governing when a company may publicly offer stock.[396] Under the Company Law, a French issuer that publicly offered securities in France is required to have the value of its outstanding capital stock paid into the issuer prior to any new issuance.[397] The new issuance is conditioned on approval by a vote at a special meeting of the issuing company's stockholders.[398] Thereafter, the issuer is subject to French securities laws to legally effectuate an offering of securities.[399]

The French securities market is regulated by the *Commission des Operations de Bourse* (COB).[400] The function of the COB is not completely analogous to the SEC.[401] The COB operates under the Ministry of Finance and is composed of five members.[402] It is less a policing authority than an overseer of market efficiency.[403] Stockbroker regulation is another significant difference between the domestic securities market and the French securities market.[404] French stock-

394. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 5-23.

395. *See* Rothwell, *supra* note 144, at 369.

396. *See* H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41 at § 7.05[2] (citing 1966 Act).

397. *See* Note, *Foreign Securities Offerings*, *supra* note 212, at 557. Any outstanding subscription fees would have to be paid in full.

398. *Id.*

399. Having complied with the requirements of French corporate laws and other applicable rules, a company can generally effectuate a public offering of its securities in France, subject to the requirements of the COB and CAC. *See* H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41, at §§ 7.01, 7.02, 7.05; *see also* Note, *Foreign Securities Offerings*, *supra* note 212, at 557.

400. *See* H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41 at § 7.01.

401. *Id.*

402. *Id.*

403. *Id.*

404. *See* H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41, at §§ 7.01, 7.02, 7.05.

brokers must be members of the *Compagnie des Agents de Change* (CAC), a stockbrokers' association.[405] The CAC elects a committee which oversees the association and enforces compliance with the rules of the association.[406] The COB functions in a managerial capacity, supervising the CAC,[407] which has greater authority and exercises control over trading.[408]

Generally, unlike trading in securities in the United States, French securities may be issued and traded in bearer form.[409] Information pertaining to the ownership of such stock is strictly confidential.[410] Furthermore, shares traded in France have a minimum par value of 100 Francs.[411] Non-par value shares may not be traded in France.[412] These permissive regulatory bodies and unusual restrictions are notable instances of departure from United States securities laws and could create difficulty in undertaking the removal of a foreign private issuer's securities from PORTAL to the Paris Exchange.[413]

Other regulatory provisions in France, however, are similar to United States law and may make compliance with United States securities laws easier. For example, a company making a public offering of its securities in France would prepare a report analogous to that filed with the SEC and file it with the CAC.[414] The report filed with the CAC must contain a description of the transaction, including the number of shares offered and the purpose for which the funds obtained in the offering will be used.[415] Concurrently, the COB reviews

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405. *Id.*

406. *Id.*

407. *Id.*

408. *See* H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41, at § 7.0. Trading in securities in bearer form, which means the identity of the owner is confidential, is common in many countries. *See* Bush, *Two Cheers*, *supra* note 124, at 37. The Internal Revenue Service has refused to change a rule which "stipulates a U.S. investor must hold securities in registered form and cannot convert that security into bearer form when selling in a secondary market." *Id.*

409. *See* H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41, at § 7.04..

410. *Id.*

411. *Id.*

412. *Id.*

413. *See* Bush, *Two Cheers*, *supra* note 124, at 37.

414. *See* H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41, at § 7.05[6]. Companies with publicly traded securities registered under French law are also subject to continuous disclosure requirements. *Id.* at § 7.09[2]; *see also* Note, *Foreign Securities Offerings*, *supra* note 212, at 550 n.54.

415. *See* H. BLOOMENTHAL, INTERNATIONAL CAPITAL MARKETS, *supra* note 41, at § 7.0.

the report and the prospectus to insure satisfactory informational disclosure.[416] The information required in the prospectus is similar to that typically required by the SEC in a public offering and includes:

1. all relevant facts concerning the transactions in question;
2. general information concerning the issuer, such as its name, juridical form, corporate purpose, registered capital and activities engaged in;
3. a description of the principal activities of the issuer, including, without limitation, information on its employees and subsidiaries;
4. certain financial information, including, without limitation, the issuer's balance sheets, profit and loss statements and consolidated accounts for the last three fiscal years as well as certain other information relating to its last five fiscal years;
5. the names of the members of the issuer's management and controlling shareholders, as well as the nature of their relationships with it;
6. a brief summary of the recent evolution of the business of the issuer and of its prospects for the future;
7. the motivation for the public offering and the use to which the proceeds therefrom are to be put; and
8. the names of the persons or legal entities responsible for disseminating the prospectus and, where appropriate, information concerning the bank or other credit establishment which guarantees the placement of the securities constituting the public offering.[417]

Undertaking such an offering may provide several additional advantages. First, Rule 144A provides a readily available resale market and access to the United States capital markets.[418] Second, a foreign private issuer structuring its offering for subsequent resale on PORTAL will be able to preserve confidentiality, deal in relationships and offer its securities in the United States more cheaply.[419] Furthermore, a foreign private issuer will not be dependent on a single market's response to its offering; its United States tranche may be removed from PORTAL and reoffered in its home country should resales under Rule 144A be less profitable than desired.[420] A foreign private

416. *Id.*

417. *Id.*

418. Fildor, *U.S. Institutions 'to expand investment'*, Fin. Times, June 15, 1990, at 36. In a Financial Times poll, a majority stated that they planned to increase their purchases of foreign securities. Miller, *New U.S. Securities Rule Threatens Euromarkets*, Fin. Times, June 1, 1990 [hereinafter Miller, *Rule Threatens Euromarkets*].

419. *See* Miller, *Rule Threatens Euromarkets*, *supra* note 418; *see also* Dash, *Private Placement Alternative*, *supra* note 20, 530-35.

420. H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 7-44; Generally, a PORTAL dealer

issuer, however, should bear in mind other applicable securities laws and restrictions before structuring a private offering with the intent to resell restricted securities pursuant to Rule 144A.

B. Initial Structuring to Reflect Resale Concerns

As mentioned in Part I of this Article, Rule 144A does not offer a foreign issuer whose securities are traded on a United States security exchange an exemption from the registration requirements of section 12 of the Exchange Act.[421] In addition, for those foreign private issuers that do not have securities registered on a national securities exchange but whose securities are nonetheless offered or sold publicly, section 12(g)(1) of the Exchange Act requires registration if the issuer has assets exceeding $1,000,000 dollars and a class of equity securities held of record by at least 500 persons.[422] Consequently, any offering subsequent to the initial private placement (i.e., an offering on PORTAL pursuant to Rule 144A) may cause certain foreign private issuers to be subject to registration with the SEC.[423]

A foreign private issuer should be aware of this possible post offering registration requirement. In a Rule 144A transaction, one way to avoid this post-registration requirement is to structure the initial transaction to control subsequent resales to qualified institutional buyers and downstream sales of its privately placed securities pursuant to Rule 144.[424] Toward this end, a foreign private issuer could build into its private placement agreements certain restrictive covenants pertaining to the number of qualified institutional buyers under Rule 144A, or purchasers pursuant to Rule 144, to whom its securities may be resold. These covenants would also include indemnification and "hold harmless" provisions if a breach of such transfer restriction results.[425] This solution may involve monitoring resales and does not resolve compliance with registration requirements should the limits imposed by section 12(g)(1) be exceeded.[426]

Rule 12g-1 of the Exchange Act provides foreign private issuers an exemption from registration under the Securities Act. This exemp-

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or broker may not effect a transfer outside of PORTAL unless certain restrictions on qualified exits are complied with and a PORTAL exit report is filed. *See* Quinn, *supra* note 14, at 83.

421. *See supra* notes 40-42 and accompanying text.

422. 15 U.S.C. § 781(a)(1988); 17 C.F.R. § 240.12g-1 (1990).

423. *See* Mooney, *Path is Cleared for Non-U.S. Issuers*, Fin. Times, May 3, 1990, at 14.

424. *See* Rothwell, *supra* note 144, at 370; *See* Dash, *Private Placement Alternative*, *supra* note 20, at 535-40.

425. *Id.*

426. 15 U.S.C. § 781(a)(1988).

tion involves subsequent offerings of the foreign issuer's securities, including offerings on PORTAL.[427] Under Rule 12g-1, if the issuer has total assets not exceeding $5,000,000, its securities are not traded on an automated inter-dealer quotation system (such as NASDAQ, but excluding trading on PORTAL), and has less than 500 holders (including PORTAL investors), then the securities are exempt from registration.[428]

Furthermore, Rule 12g3-2(a) exempts securities of a class held by less than 300 United States residents, including PORTAL investors. This exemption continues until the end of the next fiscal year in which the issuer's securities are held by more than 300 residents of the United States.[429]

The significance of section 12 of the Exchange Act to foreign private issuers indirectly involved in a Rule 144A secondary offering is that the placement of their securities in the United States may require registration should their assets or offering ever exceed limitations imposed by section 12 or Rule 12g.[430] Surpassing the limitations in downstream sales is a risk. Many foreign private issuers' assets exceed $1,000,000. Moreover, under Rule 144, a foreign issuer's restricted Rule 144A securities may be acquired by the public at the expiration of the three-year holding period without registration of securities.[431] Presumably, securities may be acquired by more than 300 persons, triggering registration under section 12 of the Exchange Act.

The risk to a foreign private issuer associated with section 12, however, may be eliminated through another exemption from section 12.[432] Rule 12g3-2(b) requires that limited information be disclosed to the SEC prior to any downstream sale if this sale would cause the offer to exceed section 12 limits and trigger registration with the

427. 17 C.F.R. § 240.12g-1; *see* Bush, *Two Cheers*, *supra* note 124, at 37. PORTAL offerings will be excluded from being an automated quotation system under Rule 12g-1. *Id.*

428. 17 C.F.R. § 240.12g-1 (1990). For purposes of Rule 12g-1, whether this $5,000,000 figure is exceeded is determined on the last day of a company's most recent fiscal year. An automated inter-dealer quotation system would include NASDAQ but would exclude PORTAL. NASDAQ, NATIONAL ASSOCIATION OF SECURITIES DEALERS MANUAL (1990), ¶ 1653a, at 1138. PORTAL investors would be calculated in the determination of the number of beneficial owners of a company's stock.

429. 17 C.F.R. § 240.12g3-2 (1990). The SEC will determine the number of securities held in the United States pursuant to Rule 12g5-1 under the Exchange Act. *Id.* at § 240.12g5-1. Securities held of record by a bank or its nominee for the account of United States residents will be counted by the number of separate accounts which hold the securities. *Id.* at § 12g3-2.

430. *See* 15 U.S.C. § 781 (1988); 17 C.F.R. § 240.12g3-2.

431. *See* 17 C.F.R. § 230.144(d)(K) (1990).

432. *Id.* at § 240.12g3-2(b).

SEC.[433] These issuers should prepare the necessary information and file in advance.

Should a foreign private issuer be eligible to use Rule 12g3-2(b), in order to qualify for the exemption such issuer would simply file with the SEC the following:

> (i) information of the issuer since the beginning of its last fiscal year (A) that has been made or is required to be made public pursuant to the law of the country of its domicile or in which it is incorporated or organized, (B) that it has filed or is required to file with a stock exchange on which its securities are traded and which was made public by such exchange, or (C) that it has distributed or is required to distribute to ts security holders;
>
> (ii) a list identifying the information referred to in paragraph [(i) *supra*] and stating when and by whom it is required to be made public, filed with any such exchange or distributed to security holders;
>
> (iii) during each subsequent fiscal year, whatever information is made public [as described in (A), (B) or (C) of paragraph (i) *supra*] promptly after such information is made or required to be made public, furnish such information;
>
> (iv) any changes that occur in the information required to be published pursuant to paragraph (ii) *supra* or any subsequent list must be provided; and
>
> (v) to the extent known or which can be obtained without unreasonable effort or expense: the number of holders of each class of equity securities resident in the United States, the amount and percentage of each class of outstanding equity securities held by residents in the United States, the circumstances in which such securities were acquired, and the date and circumstances of the most recent public distribution of securities by the issuer or an affiliate thereof.[434]

This information is usually required or provided voluntarily in a foreign issuer's home country and filing such information with the SEC should not burden the issuer.[435] For example, a French foreign private issuer whose stock is traded on PORTAL may provide the information supplied to the COB in the foreign tranche of its offering and satisfy the informational requirement of Rule 12g3-2(b). Presumably, the issuer could ascertain instantaneously the number of United

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433. *Id.*

434. *Id.*; *see also* Zaitzeff, *supra* note 38, at 64; H. BLOOMENTHAL (1990 ed.), *supra* note 2, at 5-31.

435. *See supra* notes 397-418 and accompanying text.

States security holders through PORTAL.[436]

The Rule 12g3-2(b) exemption, however, is not a panacea to all foreign private issuers subject to section 12.[437] Specifically, Rule 12g3-2(b) is not available to a foreign issuer that, during the prior eighteen months had: (i) registered under section 12 of the Securities Act or (ii) a reporting obligation (suspended or active) under section 15(d) of the Exchange Act, when these securities are quoted in an automated inter-dealer quotation system (PORTAL is currently excluded), or represented by American Depository Receipts[438] unless a grandfather provision applies.[439] Similarly, securities issued in a transaction to acquire another issuer within the same eighteen month period do not qualify for the exemption. In addition to filing certain information with the SEC, a foreign private issuer may undertake other steps prior to participating in a Rule 144A transaction.

C. Rule 144A Contract Provisions

As outlined in Part I, to offer securities among qualified institutional buyers in the United States, a foreign private issuer will place its securities pursuant to one of the statutory or regulatory exemptions available under the Securities Act.[440] During this sale the issuer and purchaser will enter into a private placement memorandum and stock purchase agreement.[441] In negotiating these agreements, covenants may be negotiated to define the rights and limitations of the parties under the Rule 144A offering.[442]

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436. *Id.*

437. 17 C.F.R. § 240.12g3-2(b) (1990).

438. *Id.*

439. 17 C.F.R. § 240.12g3-2(d) (1990). The grandfather provision enables a foreign private issuer to retroactively obtain its past compliance status with Rule 12g3-2(b) and remain eligible, despite its action under §§ 12 or 156 of the Exchange Act, to participate in the United States securities market if prior to October 5, 1983, the foreign issuers securities were traded on NASDAQ and have continuously traded on such system and continues to be in compliance with Rule 12g3-2(b). *See* Zaitzeff, *supra* note 38, at 64 (citing SEC Securities Exchange Release No. 20,265 (Oct. 6, 1983), 48 Fed. Reg. 46, 737 (1983), *reprinted in* 2 Fed. Sec. L. Rep. (CCH) ¶ 17,145, at ¶ 23,317).

440. *See supra* note 58 and accompanying text.

441. *See supra* notes 424-426 and accompanying text. Some institutional buyers will not be able to "customize" deals and, therefore, may transact their deals outside PORTAL. For example, an insurance company in a private placement does not typically employ legends on debt instruments, which is inconsistent with Rule 144A. Insurance companies also resist restrictions on resales (there is no right of the issuer to demand proof of an exemption from registration) and require on-going disclosure of information by the buyer. *See* Quinn, *supra* note 14, at 75.

442. *See supra* notes 424-426 and accompanying text. With time, standardized documentation will probably be created that will reduce the time and expense associated with such an

The most heavily negotiated provisions of the sale agreement will be the negative covenant and the registration rights provisions.[443] The foreign private issuer may seek covenants that restrict a purchaser's right to resell the issuer's securities.[444] A purchaser, on the other hand, may seek negative covenants that prohibit the foreign private issuer from affecting the purchaser's rights to liquidate its investment pursuant to Rule 144A or one of the other resale exemptions.[445]

For example, prior to the adoption of Rule 144A, securities were typically resold pursuant to Rule 144. Now, as discussed in Part I, subpart C, after the expiration of the applicable holding period, qualified institutional buyers may be able to effect a resale under Rule 144.[446] Consequently, a stock purchase agreement may contain a provision that requires certificates representing the stock to bear a legend that states: "The shares represented by this certificate have not been registered under the Securities Act of 1933 and may not be offered or sold unless an option of counsel satisfactory to the company is obtained that registration is not required."[447] This legend could be redrafted in a Rule 144A transaction to permit qualified institutional buyers to resell eligible securities under Rule 144A or pursuant to Regulation S and Rule 144.[448]

In addition to the above restrictions, restrictions on the declaration of dividends, loans or corporate mergers, the purchaser may seek prohibitions on the foreign private issuer's ability to offer additional stock to the investing public and others pursuant to a private place-

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issuance. *See* Quinn, *supra* note 14, at 70. Documentation that is presently used may be changed sufficiently to accommodate the private placements ultimate objective, to allow restricted securities to be traded on PORTAL so that buyers can buy Rule 144A securities in the secondary market. *Id.* at 74. Private placement memorandum with United States issuers, for example, may consist of public disclosure documents which incorporate recent pertinent developments with a letter describing the terms, pricing and resale restrictions of the placement. *Id.* at 72.

443. Panel Discussion, *supra* note 20.

444. *Id. See* Quinn, *supra* note 14, at 71. As previously discussed, purchasers may buy securities with the intent to resell them under Rule 144A. This will not affect the validity of a private placement. An issuer that obtains a promise from a purchaser not to resale except pursuant to Rule 144A should be able to rely on Regulation D. *Id.*

445. *See generally supra* notes 424 and 444 and accompanying text.

446. *See supra* note 424.

447. *Id.*

448. *See* Quinn, *supra* note 14, at 74. Prior to Rule 144A, resales of privately placed securities before expiration of the two or three year holding periods under Rule 144 only could be accomplished by a private placement with investment representations, appropriate legends and opinions of counsel. Resales among PORTAL investors have no such requirements. *Id.* at 68.

ment.[449] If the foreign private issuer did not take this action, the exempt status of the placement would be endangered. Under the SEC's rules of integration an additional stock offering to domestic investors may be deemed part of the same offer made to the initial purchaser. Regulation D or section 4(2) limitations may be exceeded, eliminating the transaction's exempt status.[450] This scenario may ultimately prevent the purchaser from reselling the foreign private issuer's securities.[451]

Purchasers intending to resell such securities to qualified institutional buyers may be particularly concerned about a foreign issuer's subsequent offering of equity or debt securities of the "same class," or capital stock convertible into stock of the "same class." The purchaser might try to prohibit the foreign private issuer from issuing the stock before purchase or, if the stock is issued prior to the purchase, restrict the convertability of the capital stock if the purchaser intends to eventually sell the stock to a qualified institutional buyer.

Another equally important consideration that may be reflected in the initial purchase agreement is Rule 144A's requirement that certain information about a non-reporting issuer be disclosed to the qualified institutional buyer upon request.[452] The agreement should set forth the rights of the purchaser and the qualified institutional buyer. As explained in Part II, the information required to be disclosured is not onerous. Nevertheless, to effect a Rule 144A transaction, this information should be available in case a qualified institutional buyer so requests its disclosure.[453] The language often incorporated in a stock purchase agreement in connection with the resale of securities under Rule 144 may be modified to apply to the information required under Rule 144A. Such an affirmative covenant may include an agreement by the foreign issuer to make public information available, or to comply with the reporting requirements of Rule 144A.[454]

Foreign laws, section 12 and standardization of the documentation to be used in a Rule 144A transaction are but a few of the considerations foreign private issuers and foreign banks must consider should they choose to participate in a Rule 144A transaction. Their participation, however, should not be seriously impeded by such considerations.

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449. *See supra* note 424.
450. *Id.*
451. *See* T. HAZEN, THE LAW OF SECURITIES REGULATION 104, 125-26 (1986).
452. *See SEC Rule 144A: A New Market, supra* note 20.
453. *Id.*
454. *Id.*

CONCLUSION

Rule 144A, Regulation S and PORTAL provide greater access to United States capital markets by foreign issuers. Their adoption reflects the view that United States securities markets must not be isolated from other significant foreign markets. Nor is it appropriate to exclude quality foreign offerings that might not be otherwise offered in the United States. Expansion is wise, as other foreign capital markets grow. The continued expansion of the United States securities market will most likely depend on the results achieved by the adoption of Rule 144A and Regulation S. To date, the market has not been as active as expected. The liquidity and efficiency of the private placement market created by Rule 144A may be enhanced by further modifications of Rule 144A, Regulation S and PORTAL, as well as applicable banking laws, to permit foreign private issuers and foreign banks more favorable access to the United States secondary private placement market. As Congress debates amending United States banking law to permit banks to engage in once prohibited securities activities, such proposed change offers an opportunity to remove those barriers that prevent or limit a foreign bank's use of Rule 144A.

By eliminating the "same class" prohibition under Rule 144A, the number of foreign securities eligible for trading on PORTAL, particularly equity securities, may be increased. By amending the definition of a "marketable security," foreign banks and their affiliates may be able to participate as qualified institutional buyers under Rule 144A. Such actions may facilitate a more active secondary market.