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Understand key concepts to make the most of your HC charter

By Dan Hanger

One of the primary reasons for having a bank holding company over a family owned institution is to assist ownership with estate planning. Often the mechanisms used for intergenerational ownership transfers require applications or notices to be filed with the Federal Reserve System. This article highlights some of the most common types of transactions and identifies the related regulatory filing.

Transfers to trusts

One mechanism for ownership transfers involves individuals who own shares of BHC stock transferring such shares to a trust. Since a trust is a separate entity, a transfer of BHC or bank shares to a trust can result in filing requirements under the Bank Holding Company Act and/or the Change in Bank Control Act depending upon the nature of the trust.

BHC Act considerations – If a trust is deemed to be a "company" under the BHC Act it may need to file an application to become a bank holding company depending upon the percentage of BHC or bank shares it owns. A trust will be considered to be a "company" under the BHC Act if the Federal Reserve finds that a trust is being operated as a business trust. To help determine if a trust is being operated as a business trust, the Federal Reserve reviews the nature and value of assets in the trust as well as whether the trust engages directly or indirectly in any business activities. Also, the absence of a clause requiring the trust to terminate within 21 years and 10 months after the death of grantors or beneficiaries of the trust living on the effective date of the trust or within 25 years will result in the trust being considered a "company."

CIBC Act considerations – If a trust is not considered to be a "company" under the BHC Act, it is subject to the requirements of the CIBC Act. Any person (or persons acting in concert, a concept discussed later in this article) acquiring control of a BHC or state member bank must give prior notice to the Federal Reserve. This requirement also applies to trusts and their trustees. A notice under the CIBC Act is required when a person (or persons acting in concert) would own, control, or hold with power to vote 25 percent or more of the voting shares, or 10 percent or more of the voting shares and no other shareholder controls more shares.

In practice, the Federal Reserve Board exempts some transfers from individuals to living trusts from the notice requirements of the CIBC Act if the transfer meets certain criteria.

Because a trust's status under the BHC Act and CIBC Act requires a close review of the trust instrument and its assets, we encourage individuals to contact staff of the Applications section prior to transferring shares to a trust. We can then decide if the circumstances warrant reviewing the trust to determine whether any issues are raised under either the BHC Act or the CIBC Act.

Acting in concert

One aspect of the CIBC Act that frequently raises questions relates to the application of the concept of "persons acting in concert." The Federal Reserve Board has defined rebuttable presumptions of concerted action. As a practical matter, it is very difficult to rebut one of these presumptions successfully. The most applicable presumptions for estate planning are the following:

• An individual and the individual's immediate family ("immediate family" is defined broadly in the regulation)

• A person and any trust for which the person serves as trustee

• A company and any controlling shareholder, partner, trustee, or management official of the company if both own voting securities of the banking organization

• A person joining a control group is subject to the CIBC Act and may be required to file a notice of change in control to join the control group.

Gifting

The Federal Reserve has received questions about filing or notification requirements when a BHC shareholder transfers shares via a gift. In general, the acquisition of voting securities as a bona fide gift is exempt from the prior notice requirements of the CIBC Act. Notice should be given to the Reserve Bank within 90 calendar days after the acquiring person has either acquired control of the banking organization or joined a group that controls the banking organization as a result of a gift. Depending on the facts of the specific situation, the Reserve Bank may request an after-the-fact notice of change in bank control or potentially no additional information.

Non-voting common stock

Finally, controlling shareholders sometimes use non-voting common stock as an estate planning tool. The Federal Reserve is aware of situations where this practice has resulted in non-voting common stock becoming the largest element of a BHC's equity capital. The Board's Capital Adequacy Guidelines provide that voting common stock should generally be the dominant element in Tier 1 capital; the guidelines further state that banking organizations should avoid over-reliance on non-voting elements in Tier 1 capital. These guidelines explicitly apply to BHCs with consolidated assets exceeding $500 million and to smaller BHCs meeting certain criteria (such as significant nonbanking or off-balance-sheet activities). Small BHCs are strongly encouraged to maintain capital structures that are in compliance with the guidelines. BHCs seeking to expand will find that their acquisition proposals raise financial issues and may face processing delays if their capital structure relies overly on other elements besides voting common stock.

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