No. 23-670

In the Supreme Court of the United States

MARC S. KIRSCHNER, solely in his capacity as Trustee of the Millennium Lender Claim Trust,

Petitioner,

v.

JP MORGAN CHASE BANK, N.A., JP MORGAN SECURITIES LLC, CITIBANK, N.A., BANK OF MONTREAL, BMO CAPITAL MARKETS CORP., SUNTRUST ROBINSON HUMPHREY, INC., SUNTRUST BANK, CITIGROUP GLOBAL MARKETS, INC.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF AMERICANS FOR FINANCIAL REFORM EDUCATION FUND AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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January 22, 2024

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INTEREST OF *AMICUS CURIAE*[1]

Amicus curiae Americans for Financial Reform Education Fund, "the leading voice for Wall Street accountability on Capitol Hill,"[2] is a nonpartisan and nonprofit coalition of over 200 civil rights, consumer, labor, business, investor, faith-based, civic, and community groups. Launched in the 2008 financial crisis's wake, AFREF seeks to build a strong, stable, and ethical financial system that serves the nationwide economy. Its vision is a world in which the rules governing the economy justly and sustainably focus on human needs and help all families and communities thrive. To that end, AFREF routinely submits comment letters to regulators and government entities such as the CFPB, CFTC, Department of Labor, Department of Justice, Federal Reserve, and SEC, among others; it also submits *amicus* briefs in litigation with significant economic impacts like this one.

AFREF is keenly interested in this case because the issue whether securities laws protect investments in modern syndicated loans has significant economic implications for families and communities that invest through pensions, mutual funds, or ETFs. The syndicated loan market recently eclipsed $3 trillion, rapidly approaching the $15 trillion market for corporate bonds, which all agree are securities. Thus, any ruling

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[1] The parties were timely notified of the filing of this brief, no party's counsel authored this brief in whole or in part, and no person or entity, other than *amicus* and its counsel, made any monetary contribution to its preparation or submission. *See* S. Ct. R. 37.2, 37.6.

[2] Zachary D. Carter, *House Votes to Audit the Fed... and Deregulate Wall Street*, Huffington Post (Sept. 17, 2014), *at* https://tinyurl.com/yz5v7a5b.

here would significantly impact how business entities raise capital and the extent to which regulators and securities laws protect investors.

This case presents important securities issues worthy of consideration: whether the notes supporting syndicated loans qualify as securities and whether the Court should revisit the family resemblance test of *Reves v. Ernst & Young*, 494 U.S. 56 (1990). At minimum, the Court should call for the views of the Solicitor General.

SUMMARY OF ARGUMENT

In the 1980s, courts agreed that *traditional* loan participations, in which a lead bank makes a loan to a corporate borrower and then sells all or portions of that note to a handful of other banks, didn't qualify as securities. But in the 1990s, the financial landscape changed, and the question became whether *modern* loan participations, in which a lead bank makes a loan to a corporate borrower and then sells all or portions of that note to a handful of other banks plus non-bank investors, qualify as securities.

Applying *Reves*, the court of appeals then held they also weren't securities. *Banco Español de Credito v. Sec. Pac. Nat'l Bank*, 973 F.2d 51, 54–56 (2d Cir. 1992). Alas, it arrived at that result over dissent and despite the SEC's objections. *Id.* at 56 (Oakes, C.J., dissenting); C.A. Docs. 213.7–8 (SEC's *amicus* briefs).

During certiorari proceedings, this Court called for the views of the Solicitor General, whose *amicus* brief ultimately disavowed numerous aspects of *Banco Español* as errors "open to serious question." C.A. Doc. 213.9 at 16 (Solicitor General's *amicus* brief). In particular, he explained, *Banco Español* "erred" in

(1) "the significance it attached to the fact that the notes were sold only to supposedly sophisticated institutions, and not individuals" and (2) "concluding that the mere existence of banking guidelines for the purchase of loan participations weighs against the conclusion that loan participations are securities." *Id.* Certiorari was denied. *Banco Español de Credito v. Sec. Pac. Nat'l Bank*, 113 S. Ct. 1042 (1993). In the decades since, legal academics have subjected *Banco Español* to withering criticism. *See infra* note 4.

Perhaps emboldened by *Banco Español*, the financial landscape has changed once again. Dissatisfied with selling loan participations, banks concocted an altogether new financial instrument: the loan syndication. This time, instead of selling the original note itself primarily to a handful other banks, a lead bank would now issue a new note and sell it to hundreds of non-bank investors. That market has grown geometrically from $497 billion in 2010 to $3 trillion in the present day, leading to the instant dispute.

In the court of appeals, the parties comprehensively and thoughtfully briefed whether Millennium's $1.775 billion syndicated loan, which was julienned into hundreds of slices and distributed to over 400 investors—only one of which might be a bank[3]—was a security. Naturally, their arguments focused on what *Reves* and *Banco Español* had meant. As an *amicus* below, AFREF argued *Banco Español* should be overruled. C.A. Doc. 165 at 14.

Instead, the court of appeals not only held fast to *Banco Español*, but extended its application from loan participations to loan syndications. But as the SEC,

[3] Specifically, Deutsche Bank AG-Cayman Islands Branch appears to be a foreign bank.

Chief Judge Oakes, and the Solicitor General then recognized (and as legal academics still complain), *Banco Español* was wrong when it was decided. Subsequent developments have undermined it even further. Now, the Court should intervene to uproot this mistaken line of precedent.

Modern syndicated loans allow banks to evade securities laws and non-banks to evade banking laws. Congress didn't intend to allow this $3 trillion market to evade securities regulation.

ARGUMENT

I. *Banco Español* and the decision below have been erected upon a faulty foundation

The issues are important, and the decision below is wrong, so the Court should grant the petition or, at minimum, call for the views of the Solicitor General.

1. From inception, *Banco Español* was always controversial and far from unanimous. During its appellate briefing, the SEC repeatedly argued that the unique loan participation at issue was a security. C.A. Docs. 213.7–8. Even after the majority revised its opinion in response to a rehearing petition and the SEC's criticisms, Chief Judge Oakes still criticized it for "misread[ing] the facts, mak[ing] bad banking law and bad securities law, and stand[ing] on its head the law of this circuit and of the Supreme Court in *Reves v. Ernst & Young*." 973 F.2d at 56 (Oakes, C.J., dissenting). During certiorari proceedings, the Solicitor General disavowed numerous aspects of *Banco Español* as errors "open to serious question." C.A. Doc. 213.9 at 16. And in the decades since, legal academics

have subjected *Banco Español* to withering criticism.[4] But to better appreciate *Banco Español*'s flaws, one must first understand how securities have been policed for the past century.

For almost a century, regulators and courts have struggled how to define a security with precision. Casting wide nets, the Securities Act and Securities Exchange Act set forth lengthy definitions. *See* 15 U.S.C. § 77b(a)(1), § 78c(a)(10). Deluged by those texts, this Court acknowledged Congress "did not attempt precisely to cabin the scope of the Securities Acts." *Reves*, 494 U.S. at 949. Rather, Congress "painted with a broad brush" while "recogniz[ing] the virtually limitless scope of human ingenuity, especially in the creation of 'countless and variable schemes devised by those who seek the use of the money of others on the promise of profits.'" *Id.* (citation omitted).

Here, the key legislative actions to understand include parts of the New Deal legislation, such as the Banking Act of 1933, the Securities Act of 1933, and

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[4] *E.g.*, Richard Y. Roberts & Randall W. Quinn, *Leveling the Playing Field: The Need for Investor Protection for Bank Sales of Loan Participations*, 63 Fordham L. Rev. 2115, 2121–25, 2129–31 (1995) (criticizing *Banco Español*); Elisabeth de Fontenay, *Do the Securities Laws Matter? The Rise of the Leveraged Loan Market*, 39 J. Corp. L. 725, 749–51 (2014) (criticizing *Banco Español* as "puzzling," "cursory," "misleading," and potentially "wrongly decided at the time"); John C. Cody, Note, *The Dysfunctional "Family Resemblance" Test: After Reves v. Ernst & Young, When Are Mortgage Notes "Securities"?*, 42 Buff. L. Rev. 761, 786 n.139 (1994) ("*Banco Español* has been widely criticized" (collecting authorities)); Robert F. Kornegay, Jr., *Bank Loans as Securities: A Legal and Financial Economic Analysis of the Treatment of Marketable Bank Assets Under the Securities Acts*, 40 UCLA L. Rev. 799, 840–49 (1993) (*Banco Español* was "wrongly decided").

the Securities Exchange Act of 1934, and more recently the repeal of the Banking Act's separation of commercial banking from investment banking and the Dodd-Frank Act of 2008 (including its so-called Volcker Rule prohibition against banks holding securities). Similarly, the key judicial actions to understand include efforts to define securities in various contexts. And practically, it's important to understand the essentially unregulated $3 trillion syndicated loan market's sheer size.

2. Before the Great Crash of 1929, there was essentially no federal regulation of securities. *See* de Fontenay, *supra* note 4, at 726 n.1. Rather, securities regulation, such as it was, had been left to state blue sky laws. Cody, *supra* note 4, at 786 n.139.

That state-centric model of regulation changed dramatically due to the Great Crash of 1929 and the Great Depression. In response, Congress began federalizing securities regulation through New Deal legislation. *See SEC v. Capital Gains Rsch. Bureau, Inc.*, 375 U.S. 180, 186 (1963). Alongside the Banking Act of 1933 (often called the Glass-Steagall Act), other important statutes were the Securities Act of 1933 and the Securities Exchange Act of 1934. *See id.*

"A fundamental purpose, common to these statutes, was to substitute a philosophy of full disclosure for the philosophy of *caveat emptor* and thus to achieve a high standard of business ethics in the securities industry." *Id.* It "'requires but little appreciation … of what happened in this country during the 1920s and 1930s to realize how essential it is that the highest ethical standards prevail' in every facet of the securities industry. *Id.* (quoting *Silver v. NYSE*, 373 U.S. 341, 366 (1963)).

Targeting banks, the Banking Act erected a wall of separation between commercial banking and investment banking. *See Sec. Indus. Ass'n v. Fed. Reserve Sys.*, 839 F.2d 47, 49, 54–56 (2d Cir. 1988). Targeting issuers of securities in the primary market, the Securities Act required registration of certain securities along with disclosures of material information. *See Capital Gains Rsch. Bureau, Inc.*, 375 U.S. at 186. Targeting securities transactions in secondary markets, the Securities Exchange Act regulated how exchanges operate. *See id.*

Crucially, both the Securities Act and the Securities Exchange Act set forth definitions of a "security." For instance, in relevant part, the Securities Act's 145-word definition of a security includes "any note, stock, … investment contract, … or, in general, any interest or instrument commonly known as a 'security.'" 15 U.S.C. § 77b(a)(1). Similarly, in relevant part, the Securities Exchange Act's 181-word definition of a security includes "any note, stock, … investment contract, … or, in general, any interest or instrument commonly known as a 'security.'" *Id.* § 78c(a)(10). Unlike the Securities Act, the Securities Exchange Act also specifies that its definition of a security "shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months." *Id.*[5]

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[5] In 1999, Congress largely repealed the Banking Act's separation of commercial banking from investment banking. *See Bd. of Trustees of Aftra Ret. Fund v. JPMorgan Chase Bank, N.A.*, 806 F. Supp. 2d 662, 667 (S.D.N.Y. 2011). A decade later, in response to the financial crisis of 2008, Congress enacted the Dodd-Frank Act of 2008. *See State Nat'l Bank of Big Spring v. Lew*, 795 F.3d 48, 51 (D.C. Cir. 2015). In § 619, Congress included the so-called

3. At any rate, interpreting their supposedly identical texts, this Court has decided close issues about what qualifies as securities in foundational decisions like *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946) (investment contracts),[6] *Landreth Timber Co. v. Landreth*, 471 U.S. 681 (1985) (stock in closely held corporations), and *Reves v. Ernst & Young*, 494 U.S. 56 (1990) (promissory notes).

3.a. *Howey* held investment contracts were securities. The issue was whether "an offering of units of a citrus grove development coupled with a contract for cultivating, marketing and remitting the net proceeds to the investor" qualified as an "investment contract" subject to securities regulation. 328 U.S. at 294. Essentially, citrus companies would sell investors a grove and a service contract to cultivate it, which included a leaseback arrangement. *Id.* at 295. In return, the investors would receive "an allocation of the net profits based upon a check made at the time of picking." *Id.* at 296.

The SEC had sought to enjoin their sales because, in its view, those offerings were unregistered, nonexempt securities. *Id.* The district court denied the injunction, and the Fifth Circuit affirmed. *Id.* But this Court granted certiorari and reversed. *Id.* at 294–301.

State blue sky precedents had held an "investment contract" meant "a contract or scheme for 'the placing of capital or laying out of money in a way intended to secure income or profit from its employment.'" *Id.* at 298 (citation omitted). Thus, *Howey* held, although

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Volcker Rule, which prohibits banks from using customer funds to trade securities. *See* 12 U.S.C. § 1851.

[6] *Accord SEC v. Edwards*, 540 U.S. 389, 393–97 (2004).

Congress hadn't expressly defined the term "investment contract," it had written that phrase against the state law backdrop. *Id.*

"In other words, an investment contract … means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise." *Id.* at 298–99. As such, the "test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others." *Id.* at 301.

This economic-reality test had two obvious benefits. The first was it "permits the fulfillment of the statutory purpose of compelling full and fair disclosure relative to the issuance of 'the many types of instruments that in our commercial world fall within the ordinary concept of a security.'" *Id.* at 299 (quoting legislative history). And the second was it "embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." *Id.*

Applying that test, *Howey* held the transactions "clearly involve investment contracts." *Id.* The crux of the transactions was "an opportunity to contribute money and to share in the profits of a large citrus fruit enterprise managed and partly owned by [the citrus companies]." *Id.* In contrast, the transfer of land was "purely incidental." *Id.* at 300. As such, the transactions were subject to SEC regulation, "even though the [citrus companies'] failure [to follow securities laws] result[ed] from a *bona fide* mistake as to the law." *Id.* at 300–01.

Thus, after *Howey*, the question whether an instrument qualified as a security seemed to turn solely on a transaction's economic realities.

3.b. In *Landreth*, however, this Court threw cold water on that interpretation of *Howey*'s economic-reality test and held stock in closely held companies was a security. The issue it considered was whether "the sale of all of the stock of a company is a securities transaction subject to the antifraud provisions of the federal securities laws." 471 U.S. at 683.

A family that owned all the stock of a lumber business sought to sell it. *Id.* Before finding a purchaser, a fire heavily damaged its sawmill. *Id.* "Despite the fire, the brokers continued to offer the stock for sale." *Id.* "Potential purchasers were advised of the damage, but were told that the mill would be completely rebuilt and modernized." *Id.* Eventually, an investor purchased all the stock and assigned it to a new company. *Id.* at 683–84. Alas, the lumber business didn't live up to expectations. *Id.* After the new company went into receivership, it sued the original owners for rescission and $2.5 million in damages under securities laws. *Id.*

Granting summary judgment, the district court dismissed the complaint for lack of jurisdiction because, under the so-called "sale of business" doctrine, the stocks weren't securities. *Id.* Relying on *Howey* and another case, the district court ruled the stock wasn't a security "unless the purchaser had entered into the transaction with the anticipation of earning profits derived from the efforts of others." *Id.* at 684–85. Because "managerial control of the business had passed into the hands of the purchasers," the district court deemed the transaction to be "a commercial venture rather than a typical investment." *Id.* at 685. The Ninth Circuit affirmed. *Id.* But this Court granted certiorari and reversed. *Id.*

Landreth acknowledged that "the fact that instruments bear the label 'stock' is not of itself sufficient to invoke the coverage of the Acts." *Id.* Rather, they must also "possess 'some of the significant characteristics typically associated with' stock," such as dividends, negotiability, ability to be pledged or hypothecated, voting rights, and capacity to appreciate. *Id.* (citation omitted).

Applying that test, *Landreth* held it was "undisputed that the stock involved here possesses all of the characteristics we [previously] identified … as traditionally associated with common stock." *Id.* at 687. Additionally, the transaction's "context," which involved the sale of a corporation's stock, was "typical of the kind of context to which the Acts normally apply." *Id.* Thus, it was "much more likely" that "an investor would believe he was covered by the federal securities laws." *Id.*

Proceeding further, *Landreth* rejected the argument "that our cases require us in every instance to look to the economic substance of the transaction to determine whether the *Howey* test has been met." *Id.* at 690. Rather, "the Court has never foreclosed the possibility that stock could be found to be a 'security' simply because it is what it purports to be." *Id.* at 691. It further noted that *Howey*'s "economic reality test" was "designed to determine whether a particular instrument is an 'investment contract,' not whether it fits within any of the examples listed in the statutory definition of 'security.'" *Id.*

Finally, *Landreth* "expressly le[ft] until another day the question whether 'notes' or 'bonds' or some other category of instrument listed in the definition might be shown 'by proving [only] the document itself.'" *Id.* at 694. "We hold only that 'stock' may be viewed as being in a category by itself for purposes of interpreting the scope of the Acts' definition of 'security.'" *Id.*

3.c. In *Reves*, this Court began addressing the question left open by *Landreth* about notes. More specifically, the issue was whether an agricultural co-op's promissory notes were securities. 494 U.S. at 58. *Reves* held they were.

The 23,000-member co-op raised money by selling to members and nonmembers promissory notes payable on the holder's demand. *Id.* Those uncollateralized, uninsured notes paid variable rates of interest adjusted monthly. *Id.* at 58–59. Eventually, the co-op went bankrupt, leaving over 1,600 investors holding $10 million in unpaid notes. *Id.* at 59.

During the bankruptcy, a class of note holders sued the co-op's auditor for securities fraud in intentionally failing to follow generally accepted accounting principles, thereby inflating the co-op's assets and net worth. *Id.* At trial, the class obtained a $6.1 million judgment. *Id.* On appeal, the Eighth Circuit reversed, holding the notes weren't securities. *Id.* But this Court granted certiorari and reversed. *Id.* at 59–60.

At the outset, *Reves* recognized Congress had "painted with a broad brush" when it defined securities, recognizing "the virtually limitless scope of human ingenuity, especially in the creation of 'countless and variable schemes devised by those who seek the use of the money of others on the promise of profits.'" *Id.* at 60–61 (quoting *Howey*, 328 U.S. at 299). Thus, on one hand, Congress "did not attempt precisely to cabin the scope of the Securities Acts," but instead "enacted a definition of 'security' sufficiently broad to encompass virtually any instrument that might be sold as an investment." *Id.* at 61. On the other hand, Congress didn't "'intend to provide a broad federal remedy for all fraud.'" *Id.* (quoting *Marine Bank v. Weaver*, 455 U.S. 551, 556 (1982)).

Thus, *Reves* navigated those alternatives by acknowledging "we are not bound by legal formalisms, but instead take account of the economics of the transaction under investigation." *Id.* That's because "Congress' purpose in enacting the securities laws was to regulate investments, in whatever form they are made and by whatever name they are called." *Id.*

Unlike *Howey*, a "commitment to an examination of the economic realities of a transaction does not necessarily entail a case-by-case analysis of every instrument." *Id.* at 62. Rather, some investments, such as the stock in *Landreth*, always qualify as securities if they have the "economic characteristics traditionally associated with stock." *Id.*

In contrast, notes were different. *Id.* Although common stock is "the quintessence of a security," the same "simply cannot be said of notes, which are used in a variety of settings, not all of which involve investments." *Id.* Thus, "the phrase 'any note' should not be interpreted to mean literally 'any note,' but must be understood against the backdrop of what Congress was attempting to accomplish in enacting the Securities Acts." *Id.* at 62–63.

To assess that backdrop, *Reves* considered and rejected both the *Howey* test and the *Landreth* test. *Id.* at 63. *Landreth*'s "formula cannot sensibly be applied to notes," and *Howey*'s test was limited to determining whether an instrument is an investment contract. *Id.* at 63–64.

Instead, *Reves* considered other tests adopted by lower courts. In particular, the most palatable option, which *Reves* ultimately adopted with one modification with respect to nine-month instruments, was the "family resemblance" test. *See id.* at 64–67. Under that test, all notes are presumed to be securities. *Id.* But that presumption can be rebutted if the note bears a "strong resemblance" to a list of notes that don't qualify as securities (*e.g.*, mortgage notes, consumer financing, etc.) by considering a four-factor test.

First, "we examine the transaction to assess the motivations that would prompt a reasonable seller and buyer to enter into it." *Id.* at 66 (emphasis added). Second, "we examine the 'plan of distribution' of the instrument to determine whether it is an instrument in which there is 'common trading for speculation or investment.'" *Id.* (citations omitted). Third, "we examine the reasonable expectations of the investing public." *Id.* Finally, "we examine whether some factor such as the existence of another regulatory scheme significantly reduces the risk of the instrument, thereby rendering application of the Securities Acts unnecessary." *Id.* at 67 (emphasis added).

Applying that test, *Reves* held the co-op's promissory notes were securities. First, the co-op "sold the notes in an effort to raise capital for its general business operations, and purchasers bought them in order to earn a profit in the form of interest." *Id.* at 67–68. Second, although the notes weren't traded on an exchange, they were offered to all 23,000 members and held by 1,600 members and nonmembers at the time of bankruptcy. *Id.* at 68. Third, the co-op's advertisements characterized the notes as investments, and "no countervailing factors … would have led a reasonable person to question this characterization." *Id.*

4. Triangulating between the tests announced in cases like *Howey* (investment contracts), *Landreth* (stocks), and *Reves* (notes), courts in the 1980s routinely held traditional loan participations weren't securities.[7] But that was a different time, and those courts were dealing with very different debt instruments that "contained features that justify the courts' decisions." Roberts & Quinn, *supra* note 4, at 2117.

"A loan participation traditionally is an arrangement by which a bank or other financial institution makes a loan to a corporate borrower and then sells all or a portion of the loan to one or more participants." *Id.* The participants in a traditional loan participation "were in the business of making loans, and the sale or purchase of loan participations was only a part of the business." *Id.* Additionally, traditional loan participations "usually involved only a handful of participants" that could realistically expect to "engage in one-to-one negotiations with the lead bank and, if they wished, could perform their own credit analysis of the borrower." *Id.* at 2117–18. In other words, participants traditionally "had substantial bargaining power and the ability to access information regarding the creditworthiness of the borrower." *Id.* at 2118. And given

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[7] *See, e.g.*, *United Am. Bank v. Gunter*, 620 F.2d 1108, 1115 (5th Cir. 1980); *Union Planters Nat'l Bank v. Com. Credit Bus. Loans, Inc.*, 651 F.2d 1174, 1181 (6th Cir. 1981); *Am. Fletcher Mortg. Co. v. U.S. Steel Credit Corp.*, 635 F.2d 1247, 1255 (7th Cir. 1980); *Union Nat'l Bank v. Farmers Bank*, 786 F.2d 881, 885 (8th Cir. 1986); *First Citizens Fed. S&L Ass'n v. Worthen Bank & Trust Co.*, 919 F.2d 510, 516 (9th Cir. 1990); *McVay v. W. Plains Serv. Corp.*, 823 F.2d 1395, 1399 (10th Cir. 1987).

those characteristics, AFREF agrees those traditional loan participations "arguably did not raise serious investor protection concerns." *Id.*

5. For the first time in *Banco Español*, however, the court of appeals extended that prior judicial approval of traditional loan participations to a modern one of a different breed altogether. Although it bore "a superficial resemblance to traditional loan participations," it "differ[ed] from those traditional participations in several important respects, including (1) who the participants are; (2) what the purposes of the purchasers or participants are; and (3) what the promotional basis used in marketing the loan notes is." 973 F.2d at 56 (Oakes, C.J., dissenting).

First, the participants weren't "commercial lenders who engage in traditional loan participations," but rather were nonfinancial entities "making an investment." *Id.* Indeed, even the few banks that purchased those notes "generally did so not through their lending departments but through their investment and trading departments." *Id.* Second, the participants were motivated by investment purposes, "not by the commercial purpose of operating a lending business in which participations are taken as an adjunct to direct lending operations." *Id.* Third, the arranger's promotional literature "advertised the so-called loan notes as competitive with commercial paper, a well-recognized security under the Securities Act, and on the basis of the return that they offered over that of other investments." *Id.*

Nonplussed, the *Banco Español* majority held the loan participation "as marketed in this case" was "analogous to the enumerated category of loans issued by banks for commercial purposes." *Id.* at 56. But leaving itself future wiggle room, the majority "recognize[d]" that the "manner in which participations" are "used, pooled, or marketed might establish that such participations are securities." *Id.*

Chief Judge Oakes dissented vigorously, asserting the majority misread the facts, made bad banking and securities law, and stood precedent on its head. 973 F.2d at 56 (Oakes, C.J., dissenting).

He explained the modern loan participation superficially resembled traditional participations, but differed in important respects regarding who the participants were, what purposes they had, and how they were promoted. *Id.* Additionally, "the scope of information available to the purchasers" was lesser, because there was no one-to-one negotiation with the lead lender or borrower or disclosure of all material nonpublic information. *Id.* at 56–57. Thus, the participants "were not in a position to approach the hundred or more possible borrowers in the program and conduct their own examinations." *Id.* at 57. Moreover, 53% of the participants "were not financial institutions." *Id.* And often daily solicited, sometimes by cold calls, the participations were promoted and distributed as liquid investments. *Id.* at 57–58. Lastly, he noted the SEC's amicus briefs had described loan participation markets as exceeding $100 billion, so it wasn't "exactly about chicken feed." *Id.* at 58. Thus, per *Reves*, he would have reversed. *Id.* at 58–60.

There was further appellate review when the participants sought certiorari. Roberts & Quinn, *supra* note 4, at 2123–24 & nn.60–69. Initially, this Court called for a response from the Solicitor General. *Id.* But the SEC disagreed with federal banking regulators what the government's position should be. *Id.* Ultimately, the SEC didn't join the Solicitor General's brief. *Id.*

Still, despite opposing certiorari given the lack of a circuit split and the potential that bank regulators might provide further guidance, the Solicitor General conceded *Banco Español* was "open to serious question." C.A. Doc. 213.9 at 16. Specifically, he admitted *Banco Español* "erred" in two respects: the first was "in the significance it attached to the fact that the notes were sold only to supposedly sophisticated institutions, and not individuals," and the second was "in concluding that the mere existence of banking guidelines for the purchase of loan participations weighs against the conclusion that loan participations are securities." *Id.* Ultimately, certiorari was denied. *Banco Español de Credito v. Sec. Pac. Nat'l Bank*, 113 S. Ct. 1042 (1993).

6. For decades, *Banco Español* has been subjected to scathing academic criticism for being puzzling, cursory, misleading, and wrongly decided. *See supra* note 4. For instance, a correct *Reves* analysis "suggests that leveraged loans, which are widely traded, highly risky investments, fit very poorly within the commercial loan framework that has until now justified their treatment as non-securities." de Fontenay, *supra note* 4, at 754. And one commentator suggested *Reves* itself is "outdated" and due for a glowup.[8]

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[8] Aidan D. Mulry, Note, *A True Sense of Security: How Kirschner v. J.P. Morgan Chase Illustrates the Failings of the Reves Family Resemblance Test and the Need to Recognize Some Syndicated Loans as Securities for the Sake of the Financial System*, 87 Brook. L. Rev. 979, 995–1003 (2022).

II. The issue is important, and the banks' concerns about securities regulation of syndicated loans are overblown

1. Today, the modern syndicated loan market eclipses $3 trillion and is growing geometrically. It grew "rapidly in the last decade" from $497 billion in 2010 to $1.2 trillion in 2018 to $1.5 trillion in 2020 to $2.5 trillion in 2022 and $3 trillion today.[9] And even the market's own terminology (*e.g.*, "par build," which describes how syndicated loans are purchased at discount and expected to appreciate in value) acknowledges most of the investor base is speculating on leveraged loans instead of extending and holding them like traditional lender/borrower relationships. *See* TwentyFour Asset Management, *"Building Par" for CLO Bondholders* (Apr. 23, 2019), *at* http://tinyurl.com/5765ddrf. Also, many banks back trading platforms to match buyers and sellers of syndicated loans in secondary markets, further reinforcing that market participants are speculating rather than extending a loan for its full term. *See* Octaura, *Octaura Completes First Fully Electronic Syndicated Loan Trades* (Feb. 1, 2023), *at* http://tinyurl.com/2hw9xhj3.

But syndicated loans aren't usually taken by financially strong companies; instead, they're typically "made to companies that have maxed out their borrowing and can no longer sell bonds directly to investors or qualify for a traditional bank loan." *See* Frank Partnoy, *The Looming Bank Collapse*, The Atlantic (July/Aug. 2020), *at* https://tinyurl.com/5dppx9r4. The lack of investor protection under securities laws for

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[9] Mulry, *supra* note 8, at 980; Joel Crank, *Rethinking Kirschner v. J.P. Morgan: How Securities and Banking Laws Should Apply to Syndicated Loans*, 93 U. Colo. L. Rev. 1095, 1099 & n.21 (2022); C.A. Doc. 143 at 11; Pet. 3.

these weaker, more heavily indebted borrowers is also repeatedly harming investors who are deceived by the asymmetric information between the loan issuer and themselves.

For instance, on July 12, 2022, JP Morgan and Goldman Sachs syndicated a $350 million loan for Avaya Holdings Corp. (a telecommunications company). But merely weeks later, Avaya warned that its previous earnings projections would miss by 60% and there was "substantial doubt about the Company's ability to continue as a going concern." Matt Wirz, *Avaya's Collapsing Debt Deal Hits Clients of Goldman, JPMorgan*, The Wall Street Journal (Aug. 9, 2022), *at* https://tinyurl.com/2hv9f9fc. Avaya officially filed for bankruptcy on February 14, 2023, and bondholders (whose holdings are subject to securities laws) sued Avaya's board of directors, alleging "massive fraud." Chris Dolmetsch, *Avaya Board Accused of "Massive Fraud" in Suit by Bondholders*, Bloomberg (Feb. 6, 2023), *at* https://tinyurl.com/s4v7y8ts.

2. If the Court is inclined to grant certiorari, the last hurdle to overcome might be the securities industry's apparent concern about potential market turmoil.

Whenever it sees a hint of regulation on the horizon, the securities industry invariably runs to courts and regulators with melodramatic, overwrought, skies-are-falling stories. *E.g.*, C.A. Doc. 143 at 14, 33 (arguing adverse ruling would "upend[] … settled expectations" and "wreak[] havoc in the vitally important market for syndicated loans" with "devastating effect" on "the lifeblood of a large sector of American business"). But honestly, Hollywood knows how to play that script much better. *See Ghostbusters* (Columbia Pictures 1984) (warning of "disaster of biblical proportions"), *at* https://tinyurl.com/p9j5sab2.

At any rate, potential market turmoil isn't a concern. First, the statutory interpretation issue is what Congress meant, not what the market wants. Indeed, *Howey*, *Landreth*, and *Reves* all ruled in favor of regulation even though each of those defendants had good-faith beliefs, based on their interpretation of prior precedents, that they weren't dealing with securities. Second, it isn't clear that market turmoil would result.[10] In fact, regulation would likely prevent market turmoil due to the threat of default rising in an essentially unregulated market. *See* Harriet Clarfelt, *Defaults on US junk loans expected to climb as rate rises squeeze earnings*, The Financial Times (Dec. 13, 2022), *at* https://tinyurl.com/33v7mwe7 (Federal Reserve's "aggressive" interest rate increases are "set to trigger a surge of defaults" in syndicated loan market). Third, even *Banco Español* left future wiggle room when it "recognize[d]" that the "manner in which participations" are "used, pooled, or marketed might establish that such participations are securities," 973 F.2d at 56, so reliance on it was always risky.[11]

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[10] The Volcker Rule implications are overblown. If syndicated loans are held to be securities, they would be exempt from the Volcker Rule insofar as banks held them in underwriting or market-making capacities. *See* 12 U.S.C. § 1851(d)(1)(B) (exempting banks from prohibition on trading securities when acting "in connection with underwriting or market-making-related activities" for "reasonably expected near term demands of clients, customers, or counterparties"); *id.* § 1851(b)(2)(A)–(B) (giving rulemaking authority to SEC and CFTC to distinguish banks' proprietary trading from market-making activities). There'd be no fire sale.

[11] Indeed, the securities industry's reliance interest is nonexistent. Even the district court recognized no court had ever blessed the notion that a syndicated loan isn't a security. Moreover, the traditional loan participation market would remain as is, because courts have correctly held those aren't securities. *See supra* note 7. And now that loans are routinely assigned, the

Fourth, nothing about disclosure of material nonpublic information is likely to change. Indeed, if the allegations are to be believed, the banks and their executives involved are lucky they aren't paying millions in restitution, forfeiture, and fines while serving life sentences for wire fraud.[12]

CONCLUSION

The petition should be granted.

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Jan. 22, 2024

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modern loan participation market no longer exists in any meaningful sense.

[12] Wire fraud, 18 U.S.C. § 1343, involves schemes to obtain money or property. *See Kelly v. United States*, 140 S. Ct. 1565, 1571 (2020). Per U.S.S.G. § 2B1.1(a)(1), (b)(1)(P), and (b)(2)(C), the guidelines calculation for a $1.775 billion scheme would be 43, which even for defendants with a spotless criminal record could equate to a life sentence under U.S.S.G. § 5A so long as a sentencing court exercised discretion to run multiple-count sentences consecutively.