



# BANKING ISSUANCE

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Comptroller of the Currency  
Administrator of National Banks

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Type: Banking Circular

Subject: Issuance of "Due Bills" to Customers  
Purchasing Securities

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TO: Chief Executive Officers of all National Banks, Deputy Comptrollers, District Administrators and all Examining Personnel

## SUMMARY

The purpose of this banking circular is to caution national banks as to the implications under the federal securities and national banking laws of certain practices involving "due bills" in securities transactions, and to set forth guidelines concerning the proper use of "due bills." In particular, national banks are cautioned that they must advise their securities customers of all material facts in connection with the issuance of "due bills", and that "due bill" activities should be conducted in compliance with the requirements of Regulation D.

## BACKGROUND

A "due bill" is an obligation that results when a bank sells any asset (including a security) and receives payment, but does not deliver the security or other asset. A "due bill" can also result from a promise to deliver an asset in exchange for value received. Outstanding "due bill" obligations, whether written or unwritten, are required to be reported as borrowings by the issuing bank in its Report of Condition, Schedule RC, item 16, under the caption "Other Borrowed Money." Conversely, when the reporting bank is the holder of a "due bill," the outstanding due bill obligation of the seller is required to be reported as a loan to that party. (See 1984 Instructions to the Reports of Condition and Income: Interim Supplement to the Glossary.)

Under the national banking laws, national banks generally are authorized to act as brokers or dealers in the purchase and sale by their customers of U.S. government securities, and Federal agency securities. When a bank sells such a security to a customer, collects the proceeds and fails to deliver the security, a "due bill" exists in favor of the paying customer. The customer, however, typically receives a confirmation from the bank stating that a security has been purchased by the customer. See 12 CFR Part 12. "Due bills" outstanding more than three business days are subject to transaction account reserve requirements under Regulation D -- Reserve Requirements of Depository Institutions, promulgated by the Board of Governors of the Federal Reserve System, unless the "due bill" is fully collateralized by securities similar to those securities that are the subject of the "due bill" transaction. See 12 CFR § 204.2(a)(1)(iv).



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## POLICY

This Office believes it appropriate to remind national banks which issue securities "due bills" to customers of the legal obligation to disclose to these customers all material facts and circumstances concerning the failure of the bank to deliver promptly the securities purchased. In addition, national banks should not accept and use in their operations customer funds remitted for security purchases without advising customers that (i) securities have not been purchased promptly for their accounts and (ii) their funds are being used by the bank. In no cases should such funds be used in operations if the securities purchased by their customers are deliverable at settlement, unless full disclosure of all material facts is made to customers and the bank complies fully with Regulation D.

National banks are reminded that, with respect to their securities transactions, they are subject to the antifraud provisions of the federal securities laws. See, e.g., Section 17(a) of the Securities Act of 1933 (15 U.S.C. § 77q(a)); Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78j(b)) and Rule 10b-5 promulgated thereunder by the SEC (17 C.F.R. § 240.10b-5). Further, if a bank undertakes to act as a broker or dealer in securities and to hold itself out to the Public as such, it is required to adhere to high standards of professional conduct in these activities. In this regard, banks should be aware that a firm in the business of acting as a broker or dealer impliedly represents that it will deal fairly with its securities customers. This implied representation includes the representation that a securities transaction placed by a customer with a broker-dealer will be consummated promptly unless there is a clear understanding to the contrary. See, Securities and Exchange Commission ("SEC"), Securities Act Release Nos. 9459 (January 14, 1972); 8363 (July 29, 1968); and 6778 (April 16, 1962).

The issuance or a "due bill" by a bank constitutes a failure to consummate promptly a securities transaction for a customer. This failure is material information which must be disclosed to the customer. Accordingly, a bank dealer which accepts a customer's securities purchase funds or order, under circumstances where the dealer is unable to consummate the transaction promptly, must advise the customer of this fact. If it fails to do so, it is failing to disclose to the customer material information concerning the customer's securities purchase; such conduct may constitute a violation of the antifraud provisions of the federal securities laws noted above.

In addition, if a national bank knowingly takes a customer's securities purchase funds and uses those funds in its general operations, instead of effecting promptly the customer's purchase order, it similarly must advise the customer of this fact. If the bank fails to do so, it compounds its failure to disclose material information to its customer and may be engaged in a fraudulent



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securities practice known as "bucketing". Further, a "due bill" which is created for the account of a customer, under circumstances where the security which is the subject of the "due bill" can be obtained and delivered at settlement, should not be treated as a bona fide "due bill" within the meaning of the transaction account reserve requirements of Federal Reserve Board Regulation D; hence, appropriate transaction account reserves must be established upon the creation of such a "due bill."

In the view of this Office, however, "due bill" transactions where the underlying security can be delivered at settlement are not an appropriate banking practice and should be discontinued, unless the bank is prepared to make prompt and full disclosure of all material facts and circumstances to the customer, and comply with Regulation D. Absent such disclosure and compliance, the issuance of "due bills" by national banks is to be limited to those situations where a security purchased by a customer cannot be delivered by the bank to the customer at settlement, notwithstanding a diligent, good faith effort by the bank to secure that security for the customer.

In view of the foregoing, national banks are advised that the policy of this Office with respect to securities "due bills" is as follows:

- Ⓒ In order to satisfy their disclosure obligations under the federal securities laws, national banks are required to make full written disclosure of all material facts and circumstances concerning any "due bills" created as to securities purchased by their customers. Such disclosure must be made in a timely manner, i.e., within one business day of the creation of a "due bill" or as soon as a bank becomes aware that it will not effect delivery of the security at settlement, whichever is sooner. This disclosure ordinarily would include:
- a description of the nature of the transaction;
  - a notice of the rights and liabilities of both parties to the transaction, including who is entitled to any interest on the underlying security;
  - the reasons for the due bill;
  - a description of the collateral (if any);
  - a statement indicating that to the extent the market value of the collateral is insufficient, the customer may be an unsecured creditor of the bank; and



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- a statement that describes what continuing steps the bank is taking to effect delivery of the security.
- Ⓒ Banks are to issue "due bills" only in those situations where the bank, despite a diligent good faith effort, is unable to deliver the security purchased by the customer at settlement, unless prompt and full disclosure of all material facts (including but not limited to the fact that the bank is taking customers' purchase funds and using these funds in the bank's operations instead of purchasing the securities ordered) is made to affected customers, and the bank complies fully with Regulation D.
- Ⓒ Under no circumstances shall a bank send a "due bill" customer any document (such as a safekeeping receipt) which has the potential to mislead the customer into believing that a security has been acquired for the customer's account, until such time that the actual security is delivered for the account of the customer.
- Ⓒ In order to ensure their continuing compliance with relevant provisions of the federal securities and national banking laws, banks are advised to adopt written policies and procedures concerning the use of "due bills."

In sum, the improper use by banks of "due bills" or the failure to make adequate disclosure to customers in connection with "due bill" transactions may result in, among other things, violations of the antifraud provisions of the federal securities laws, and deposit reserve deficiencies within the meaning of Regulation D. The obligation to make full disclosure in connection with "due bill" activities becomes all the more important where "due bills" are created in sales to retail securities customers who may not fully understand the nature and significance of these transactions. This office has taken and will take enforcement action against banks which fail to make adequate disclosure, or make misleading disclosure, concerning "due bill" transactions, or otherwise misuse "due bills". Further, this Office will carefully consider public disclosure of any enforcement actions taken with respect to "due bill" transactions pursuant to its general authority to disclose publicly enforcement actions taken with respect to national banks.



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## ORIGINATING OFFICES

Questions regarding this banking circular may be directed to the Investment Securities Division, (202) 447-1901 or the Securities and Corporate Practices Division, (202) 874-4660.

H. Joe Selby  
Senior Deputy Comptroller  
for Bank Supervision