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SHEARMAN & STERLING LLP

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I. INTRODUCTION

In response to turmoil in the financial markets, a number of governments throughout Europe have taken steps to ensure that their banks have the funds necessary to recapitalise and maintain lending in tight credit markets. One such measure employed by several countries has been to guarantee certain liabilities of eligible financial institutions, including certain types of debt securities issued by financial institutions in the international capital markets.[1] The guarantee arrangements differ markedly from country to country along the lines of which banks are eligible to participate, the duration of the guarantee, and the types of securities covered.

Such offerings of debt securities to investors in the United States by foreign private issuers[2] benefiting from sovereign guarantees raise a number of interesting issues under the U.S. federal securities laws. These laws apply to "securities" within the meaning of Section 2(a)(1) of the U.S. Securities Act of 1933 (the "Securities Act"), including "notes", "bonds", "debentures", "evidences of indebtedness" and, crucially, "guarantees of any of the foregoing". Consequently, the offer and sale of debt securities issued by financial institutions benefiting from sovereign guarantees include an offer and sale of both the debt securities by the issuer (primary obligor) and an offer and sale of the guarantee, a separate security, by the sovereign guarantor.

This publication summarises recently announced European bank debt guarantee programmes and outlines selected legal issues relating to the combined offering of corporate debt securities coupled with sovereign guarantees to investors in the United States. In particular, this publication discusses the type of sovereign disclosure required in the offering documents of the issuing financial institutions and the alternative methods of compilation, preparation and dissemination of such disclosure. It also discusses the scope of liability of the offering participants for material misstatements or omissions in such sovereign disclosure, including a discussion of whether the sovereign disclosure is "expertised" and how that determination affects due diligence procedures on the sovereign disclosure. Moreover, it addresses implications of the sovereign guarantees for documentation used in U.S. debt offerings by European financial institutions. Finally, it summarises the programme of guarantees offered by the U.S. Federal Deposit Insurance Corporation ("FDIC") to debt securities issued by U.S. financial institutions and the legal framework under the EU Prospectus Directive (the "Prospectus Directive")[3] for securities offerings made

[1] To date, the following European countries have guaranteed, in various forms, non-retail debt obligations issued by financial institutions: Austria, Belgium, France, Germany, Ireland, Italy, Portugal, Spain, The Netherlands, and the United Kingdom.

[2] Under Rule 405 under the Securities Act, the term "foreign private issuer" means any "foreign issuer" other than a foreign government except an issuer meeting the following conditions:

(1) More than 50% of the outstanding voting securities of such issuer are directly or indirectly owned of record by residents of the United States; and

(2) Any of the following: (i) the majority of the executive officers or directors are U.S. citizens or residents; (ii) more than 50% of the assets of the issuer are located in the United States; or (iii) the business of the issuer is administered principally in the United States.

The term "foreign issuer" means any issuer which is a foreign government, a national of any foreign country or a corporation or other organisation incorporated or organised under the laws of any foreign country.

[3] Directive 2003/71/EC of the European Parliament and of the Council of November 4, 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC.

with the benefit of FDIC guarantees to investors in the European Economic Area ("EEA").

This publication does not purport to be a detailed description or analysis of all of the disclosure-related and other issues resulting from unregistered offerings of sovereign-guaranteed bank securities into the United States or into the EEA. Interested persons should feel free to contact any of the Shearman & Sterling LLP attorneys listed at the end of this publication.

II. SELECTED EUROPEAN GUARANTEE PROGRAMMES

A. United Kingdom[4]

On October 8, 2008, the U.K. government announced the 2008 Credit Guarantee Scheme (the "U.K. Guarantee Programme"). Institutions eligible to participate include U.K.-incorporated banks (including U.K.-incorporated subsidiaries of foreign institutions) that have a substantial business in the United Kingdom and U.K. building societies. In addition, the eligible institution must have raised or committed to raise Tier 1 capital in the amount and form that the U.K. government considers appropriate. Instruments eligible to be guaranteed include certificates of deposit, commercial paper, and senior unsecured bonds and notes issued within the next six months for a term of three years or less. On 13 October, HM Treasury (the "U.K. Guarantor") executed and made available the programme's Deed of Guarantee, which provides that when a guaranteed issuance is not repaid by the issuer, the U.K. Guarantor shall, in accordance with rules that are to be published from time to time and following any applicable grace period, pay the guaranteed liability.[5]

[4] A Market Notice providing the operating parameters of the guarantee programme has been issued by the United Kingdom Debt Management Office and can be found at: http://www.dmo.gov.uk/documentview.aspx?docname=cgs/press/mktnotice08.pdf&page=.

[5] The Deed of Guarantee can be viewed at: http://www.dmo.gov.uk/documentview.aspx?docname=cgs/press/cgsdeed.pdf&page=.

The guarantee under the U.K. Guarantee Programme will be available in respect of eligible instruments fulfilling the following criteria ("Eligible Liabilities"):

i. senior unsecured debt instruments with standard market terms, not being complex instruments, comprising certificates of deposit, commercial paper, bonds or notes, whether issued under a programme or on a stand-alone basis;

ii. to be issued on or after October 13, 2008 and before (x) April 9, 2009 or (y) not less than seven days before April 13, 2012, provided that such liabilities are issued solely for the purpose of refinancing a guaranteed liability on the date of its scheduled maturity;

iii. the instruments must be issued within 30 days of the date of the Eligibility Certificate to be issued by the U.K. Guarantor;

iv. having a scheduled maturity date falling before April 13, 2012 (or any later date determined by the U.K. Guarantor in its sole discretion);

v. single currency denominated in sterling, euro or U.S. dollars;

vi. not to contain (x) an event of default constituted by cross-default or cross-acceleration or (y) any right of prepayment by the issuer; and

vii. the proceeds of the issue are to be applied in refinancing liabilities of the issuer (or a company directly or indirectly wholly owned by the issuer and incorporated in the United Kingdom) maturing after the date of commencement of the U.K. Guarantee Programme (October 13, 2008).

Banks that opt into the U.K. Guarantee Programme must pay the U.K. government a fee on guaranteed issuances equal to 50 basis points plus 100% of the institution's median five-year credit default swap spread during the 12 months to October 7, 2008. Banks currently listed as eligible for this programme are Abbey, Barclays, HBOS,

HSBC, Lloyds-TSB, Royal Bank of Scotland, Standard Chartered and Nationwide, a large building society.

The initial application period is from October 13, 2008 to April 9, 2009 (the "Final Application Date"). The Final Application Date may be extended by the U.K. Guarantor in its sole discretion. The decision to issue Eligibility Certificates is at the U.K. Guarantor's discretion.

Under the terms of the Deed of Guarantee, the U.K. Guarantor irrevocably guarantees the payment by the issuer of liabilities in respect of which an Eligibility Certificate has been issued ("Guaranteed Liabilities"); and undertakes with the beneficiaries of such liabilities that if the issuer does not pay any Guaranteed Liability on the date on which it becomes due and payable, it shall, on demand and following any grace period, pay that Guaranteed Liability.

The U.K. Guarantor will not be liable under the Guarantee in respect of any Guaranteed Liability "which has been varied, amended, waived, released, novated, supplemented, extended or restated in any respect without the prior written consent of the Guarantor". Because the definition of "Guaranteed Liabilities" refers to "any liability", it is arguable that this prohibition does not extend to amendments which do not affect the "liability", e.g meetings provisions.

A list of debt securities guaranteed under the UK Guarantees Programme, identified by their International Securities Identification Number (ISIN), will be made available at website of the U.K. Debt Management Office at www.dmo.gov.uk. As of the date of this publication, there has been one instrument guaranteed under this programme (ISIN: XS0395325144).

B. Germany

The German Financial Markets Stabilisation Act ("Stabilisation Act") was published in the Federal Law Gazette (*Bundesgesetzblatt*) (BGBl. I, p. 1981) on October 17, 2008 and came into force on October 18, 2008. The main purpose of the Stabilisation Act is to restore and sustain confidence and liquidity in the German financial market. Under the Stabilisation Act, a "Financial Markets Stabilisation Fund" (*Finanzmarktstabilisierungsfonds*; "Stabilisation Fund") will be set up by the federal state (*Bund*). The Stabilisation Fund is set up as a special fund (*Sondervermögen*) of the federal state and does not have its own legal personality (*nicht rechtsfähig*). The liabilities of the Stabilisation Fund will be guaranteed by the federal state (*Bund*). The Stabilisation Fund is authorised to: (i) recapitalise companies in the financial sector, (ii) guarantee certain bonds, debentures and deposits, and (iii) purchase certain assets.

The details relating to such measures under the Stabilisation Act are set out in the regulation regarding the implementation of the Financial Markets Stabilisation Fund Act (*Finanzmarktstabilisierungsfonds-Verordnung*; "Stabilisation Fund Regulation"), which was published by the government under the Stabilisation Act and came into force on October 20, 2008.

Pursuant to the Stabilisation Act and the Stabilisation Fund Regulation, the Stabilisation Fund may guarantee bonds, debentures and deposits, each with a maturity of up to 36 months, issued by financial sector companies after October 17, 2008 and before December 31, 2009. Guarantees shall expire no later than December 31, 2012. The purpose of this measure is to provide financial sector companies with access to liquidity and to facilitate refinancing in the capital markets. The aggregate volume of guarantees provided by the Stabilisation Fund is limited to €400 billion; the limits of guarantees for individual financial sector companies will depend on their respective capital endowment.

Guarantees shall generally be issued in the form of guarantees on first demand (*Garantie auf erstes Anfordern*) and shall generally only be granted if the concerned financial sector company is equipped with adequate funds (*angemessene Eigenmittelausstattung*). The Stabilisation Fund shall receive adequate consideration for the granting of guarantees, which will generally consist of a certain percentage of the maximum guarantee amount reflecting the default risk plus a margin. Currency risks of guarantees are to be hedged at the expense of the concerned financial sector company.

The Stabilisation Act applies to companies within the financial sector and with their seat (*Sitz*) in Germany. Financial sector companies in the meaning of the Stabilisation Act include credit institutions (*Kreditinstitute*), financial services institutions (*Finanzdienstleistungsinstitute*), insurance companies, pension funds, investment companies (*Kapitalanlagegesellschaften*), operators of stock exchanges (*Wertpapierbörsen*) and derivates exchanges (*Terminbörsen*), parent companies of the above named companies, if they are financial holding companies (*Finanzholding-Gesellschaften*), hybrid financial holding companies (*gemischte Finanzholding-Gesellschaften*) and regulated companies that are part of a financial conglomerate (*beaufsichtigte Finanzkonglomeratsunternehmen*). German *Landesbanks* also qualify as financial sector companies under the Stabilisation Act. Subsidiaries of foreign banks that are licensed in Germany are also covered by the Stabilisation Act.

Companies seeking assistance under the Stabilisation Act must file an application with the Financial Stabilisation Institution. Access and details of the requested measures are in the discretion of the Financial Stabilisation Institution; companies have no legal right to obtain assistance under the Stabilisation Act. The discretionary decision has to be made under consideration of the importance of the company for the stability of the financial markets, the urgency of the matter and the effective economic distribution of the Stabilisation Funds' assets.

Access to the measures under the Stabilisation Act may be subject to detailed requirements, which are outlined in the Stabilisation Fund Regulation and will be determined on a case-by-case basis according to the kind, volume and duration of the stabilisation measures as well as the economic situation of the relevant financial sector company. As a general rule, the requirements to be imposed shall ensure the sound and prudent management of the company.

The particular requirements to be imposed on a beneficiary company will depend on the type of stabilisation measure. In case of the issuance of guarantees, the relevant company shall be instructed to review its business policy, including for sustainability. In connection with such review the Stabilisation Fund can require the financial sector company to reduce or cease certain business activities (including activities relating to certain products or markets) which carry particular risks (including risks detailed in Annex V of the European Directive EC 2006/48).

C. France

A new law aimed at "restoring confidence in the financial and banking system and to ensuring adequate financing of the French economy" was enacted on October 16, 2008. Under this new law, a new government-backed entity (Société Française de Refinancement de l'Economie, or "SFRE") has been created, whose share capital is 34% owned by the French state and 66% owned by financial institutions.

The SFRE will issue debt securities guaranteed by the French state and then lend funds to financial institutions. Any financial institution operating in France may borrow funds through the SFRE, provided it furnishes sufficient and adequate collateral and signs an agreement with the government committing to use the capital raised to finance loans to individuals, companies and local public entities. The government may also require beneficiary companies to institute good corporate governance practices.

On an exceptional basis and, in particular, in cases of emergency, the French state may directly guarantee securities issued by financial institutions, provided the French state is assured sufficient collateral. In addition, the guarantee may also benefit an entity that is fully owned by the government, which will raise funds to subscribe to securities issued by financial institutions to strengthen their capital ratios. Special measures were also put in place to guarantee entities of the Dexia Group.

The state guarantee will be made available at commercial rates for debt securities issued by the SFRE or, in case of emergency, by financial institutions in distress, before December 31, 2009, and with maturities up to five years.

All the aforementioned guarantees shall not exceed €360 billion, out of which €320 billion will benefit SFRE and Dexia, according to the French Ministry of Finance.

D. Italy

On October 9, 2008, the Italian Government issued Decree Law No. 155 ("Decree No. 155"), entitled: "Urgent measures to guarantee the stability of the credit system and the continued flow of credit to firms and consumers in the current state of world financial crisis". Decree No. 155 contains the following principal provisions:

- It empowers the Ministry for Economy and Finance ("MEF") to subscribe for or guarantee capital increases effected by Italian banks, provided that such banks adopt a stabilisation plan approved by the Bank of Italy. All shares subscribed by MEF will benefit from a priority in dividend distribution.
- It simplifies the rules regarding the collateral required to be posted by banks that request financing from the Bank of Italy.
- It authorises MEF to guarantee loans granted by the Bank of Italy to Italian banks and the Italian branches of foreign banks in the event of a "severe liquidity crisis".
- It empowers MEF to backstop the Italian interbank deposit insurance scheme and increases the coverage level of deposit insurance to €103,191.38 per account (more than double the minimum level in the European Union ("EU"), which was recently raised to €50,000).

On October 13, 2008, the Government issued Decree Law No. 157 ("Decree No. 157"), entitled: "Additional urgent measures to guarantee the stability of the credit system". Decree No. 157 implements the measures agreed with the other Euro-area countries at the Ecofin meeting held on October 7, 2008 and the EU summit meeting held on October 12, 2008.

Specifically, Decree No. 157 authorises MEF: (i) to guarantee all liabilities having a maturity of less than five years issued by Italian banks after October 13, 2008 and before December 31, 2009; (ii) to effect certain temporary exchanges of government securities for financial assets held by Italian banks or liabilities of counterparty Italian banks having a maturity of less than five years issued after October 13, 2008 and before December 31, 2009; and (iii) to guarantee contracts entered into by Italian banks for the purpose of obtaining, on a temporary basis, securities eligible for use in refinancing operations within the Eurosystem.

No limit has been established for the volume of such guarantees; however, the Decree No. 157 states that all guarantees provided thereunder shall be issued at "market conditions" and shall be granted priority ranking. The Bank of Italy is tasked with assessing whether applicant banks are sufficiently capitalised to participate in this program and to meet the obligations arising therefrom.

The implementing regulations for Decree No. 155 and Decree No. 157 will be promulgated by MEF, in consultation with the Bank of Italy. MEF has stated informally that it expects to issue such rules "within a few days".

III. DISCLOSURE REQUIREMENTS

Under the Securities Act, the "offer" and "sale" of debt securities issued by financial institutions benefiting from sovereign guarantees include two legally distinct offerings, each subject to the registration and prospectus delivery requirements of Section 5 of the Securities Act and the rules and regulations thereunder: (i) an offer and sale of the debt securities by the issuer (primary obligor), and (ii) an offer and sale of the guarantee, a separate security, by the sovereign guarantor. Neither the offer and sale of the corporate securities nor the offer and sale of the sovereign guarantees may be extended to investors in the United States without registering such offerings under the Securities Act or perfecting one of the available exemptions from registration, such as the resale

exemption provided by Rule 144A under the Securities Act ("Rule 144A").[6]

In a registered offering, Section 7(a) of the Securities Act provides that the registration statement for the offering of the corporate debt security must respond to the disclosure requirements of the relevant corporate disclosure form under the Securities Act, whereas the registration statement relating to the corporate guarantee must contain the information, and be accompanied by the documents, specified in Schedule B under the Securities Act ("Schedule B"). In practice, the combined offering will be made pursuant to a combined registration statement that will include the relevant corporate disclosure with respect to the corporate debt security, and the sovereign disclosure (and accompanying documents) required by Schedule B with respect to the sovereign guarantor. A summary of the information required by Schedule B can be found in the Annex to this publication.

In practice, European financial institutions availing themselves of sovereign guarantees are unlikely to access the U.S. capital markets with SEC-registered public offerings of debt securities. In line with historical market practice and in the interest of fast execution, any such offering is likely to be made (i) in the United States to qualified institutional buyers within the meaning of Rule 144A[7] and (ii) outside the United States pursuant to Regulation S under the Securities Act ("Regulation S").[8] Indeed, a large number of financial institutions that will likely use the sovereign guarantee have long established medium-term-note programmes for exempt offerings of debt securities in the United States pursuant to Rule 144A to support capital raising activities in the United States from time to time.[9]

Although technically not subject to the registration and prospectus delivery requirements of the Securities Act, offerings of securities pursuant to Rule 144A and Regulation S are expected to be conducted, and are customarily conducted, on the basis of disclosure documents that are substantially responsive by analogy to the disclosure requirements of the Securities Act and the rules and regulations thereunder. Consequently, combined Rule 144A offerings of corporate debt securities coupled with sovereign guarantees will be expected to be marketed on the basis of offering disclosure documents that include, with respect to the corporate issuer, corporate disclosure that substantially meets the requirements of the Securities Act and, with respect to the sovereign guarantor, guarantor disclosure that substantially meets the requirements of Schedule B. We would emphasise that the provision of the guarantee and the inclusion of guarantor disclosure do not obviate the need for disclosure concerning the corporate issuer, which would need to be provided to the same extent as if the offering were not guaranteed.

Assuming that the relevant offering document will include guarantor disclosure substantially consistent with the requirements of Schedule B, how should such disclosure be included in the offering document and become available to potential investors? There are basically three alternatives.

First, if the sovereign guarantor has filed a registration statement under the Securities Act containing the information required by Schedule B and has since provided the periodic updates to that information

[6] Note that many of the current debt programmes used by financial institutions to offer debt securities into the U.S. are guaranteed by the corporate parent of the issuer. If an issuance under these programmes is also guaranteed by a sovereign government, the issuance would involve three separate securities. If this is the case, the discussion in this publication of disclosure requirements and diligence and liability issues concerning the issuer should also apply to the corporate guarantor.

[7] Another available exemption for financial institution issuers wishing to access the U.S. market would be an offering of short-term debt securities having a maturity at time of issuance not exceeding nine months, the proceeds of which have been or are to be used for current transactions. See Section 3(a)(3) of the Securities Act.

[8] Sovereign-guaranteed offerings that are sold pursuant to both Rule 144A and Regulation S will qualify for "category 1" treatment under Rule 903, which forms a part of Regulation S. This is true regardless of whether there is substantial U.S. market interest in the securities of either the issuer or the guarantor.

[9] Another alternative would be for the SEC to provide exemptive relief, citing extraordinary market conditions, from the registration, prospectus delivery and liability provisions under the U.S. federal securities laws with respect to issuances of debt securities with sovereign guarantees by foreign private issuers. We are somewhat sceptical that the SEC would grant this exemptive relief either across the board in respect of all EEA countries or for select EEA countries.

required by the relevant form in a timely fashion,[10] the offering document may incorporate by reference the sovereign disclosure that is already on file with the SEC and available on EDGAR.[11] Incorporation of documents by reference has long been accepted as a valid alternative for conveying material disclosure in the Rule 144A market. The information may alternatively be copied directly into the offering document.

If the sovereign guarantor is not a current Schedule B filer, the approach that the issuer should take depends on whether the sovereign guarantor has compiled and made available sovereign disclosure substantially responsive to Schedule B for use by financial institutions benefiting from the guarantee in their capital raising activities in the U.S. market (or the issuer reasonably expects that the sovereign guarantor will compile and make available such disclosure). If the sovereign guarantor has prepared and made available the required sovereign disclosure, the issuer will include (or incorporate by reference from a website maintained by the sovereign guarantor) such disclosure in the offering document.

If the sovereign guarantor has not provided this disclosure, the issuer's only other viable alternative would be to source the relevant statistical and other information from publicly available sources and compile the relevant Schedule B disclosure without assistance from, or access to, the sovereign guarantor. The issuer should accompany the Schedule B disclosure with appropriate cautionary statements to the effect that the relevant information has been compiled by the issuer without the sovereign guarantor's participation and has not been independently verified by the issuer.

Whether the inclusion of sovereign disclosure substantially similar to that required by Schedule B in the offering documents is allowed by the sovereign guarantor must also be checked through appropriate review of the applicable rules of the relevant sovereign guarantee programme. For example, in the United Kingdom, the rules set out by HM Treasury provide that, with the exception of the disclosure of the terms of the guarantee in the form provided by HM Treasury (which is limited to a brief description of the guarantee), no eligible institution shall otherwise "explicitly promote itself" on the basis of the guarantee.[12] It is unclear whether this provision would restrict the inclusion of disclosure regarding the sovereign guarantor. Given that such disclosure is necessary for a Rule 144A offering, this provision would need to be clarified before an issuer embarks on a 144A offering of guaranteed debt.[13] Generally, discussions with the relevant programme authorities should be undertaken to obtain comfort that the level of disclosure does not run afoul of programme rules.

IV. DUE DILIGENCE AND LIABILITY ISSUES

Underwriters and directors of the issuing financial institution in an unregistered offering sold into the United States have a due diligence defence against suits brought against them under the U.S. federal securities laws for an untrue statement of a material fact or for an omission of a material fact necessary in order to make the statements, in light of the circumstances, not misleading. To perfect this defence, the party must demonstrate that it conducted a reasonable investigation in the context of the offering. The standard of investigation required in order to establish a due diligence defence varies depending on the circumstances concerning the particular offering.

A. Expertisation

The standard of investigation that an underwriter must perform in order to establish a due diligence defence is lower for so-called expertised portions of the offering document. Section 11(b)(3)(C) of the Securities Act provides that a due diligence defence for a material misstatement or omission in an expertised portion of a registration statement may be sustained if the defendant

[10] Sovereigns registered under the U.S. Securities and Exchange Act of 1934 are required to file annual reports on Form 18-K. A copy of this form can be found at: http://sec.gov/about/forms/form18-k.pdf.

[11] Schedule B disclosure relating to the Federal Republic of Germany can be found on the SEC's website at: http://sec.gov/cgi-bin/browse-edgar?action=getcompany&CIK=0000821533&owner=include&count=40.

[12] The Rules of the 2008 Credit Guarantee Scheme can be viewed at: http://www.dmo.gov.uk/docs/cgs/press/cgsrules.pdf.

[13] Query whether this provision would prohibit the debt securities from being titled "guaranteed" debt securities.

can prove that he or she had no reasonable ground to believe, and did not believe, that the expertised portions of the registration statement contained materially untrue statements or omissions or failed to represent the expert's statement. Section 11(b)(3)(D) of the Securities Act provides a similar standard for sections of the registration statement containing statements made by official persons or extracts from public official documents. Court cases, however, provide that where "red flags" exists regarding the reliability of an expertised section, mere reliance on the expert is not sufficient to ward off liability.[14] The lower standard of care for expertised sections provided in these sections will apply by analogy in disputes concerning material misstatements or omissions in unregistered offerings.

It is thus critical to determine whether and to what extent country disclosure is expertised for purposes of the due diligence defence. Although there is a dearth of case law on the subject, it is reasonable to expect that portions of the disclosure that are derived from public records issued by the appropriate government authority, including statistical data from public sources concerning demographics, budget, foreign exchange, foreign trade, wages, prices and the like, will be expertised because these portions are derived from publicly available documents produced by government entities. EEA governments traditionally grant public access to most government data and it is expected that statistical data included in the offering disclosure will be derived from publicly available data and not produced specifically for the offering.

Certain disclosure, however, will likely not be expertised. This would include disclosure and the omission of material disclosure related to information not derived from public official documents. As a practical matter, this would include narrative disclosure or statistical data that is produced specifically for use in the offering and that is otherwise not publicly available in a published government release.

[14] *In re Worldcom, Inc. Sec. Litig.*, 2004 WL 2889974 (S.D.N.Y. 2004).

B. Recommended Due Diligence Procedures

The extent of due diligence that is reasonable under the circumstances is not provided by statute and depends on the circumstances of the particular offering. In Rule 176 under the Securities Act, the SEC has provided certain guidelines for what constitutes a reasonable investigation under Section 11 of the Securities Act. Rule 176 applies only to registered offerings, but the factors listed are also the factors appropriate to consider in the context of an unregistered offering. Rule 176 provides that in determining whether or not the conduct of a person constitutes a reasonable investigation, relevant circumstances include, with respect to a person other than the issuer:

- The type of issuer;
- The type of security;
- The type of person;
- The office held when the person is an officer;
- The presence or absence of another relationship to the issuer when the person is a director or proposed director;
- Reasonable reliance on officers, employees, and others whose duties should have given them knowledge of the particular facts (in the light of the functions and responsibilities of the particular person with respect to the issuer and the filing);
- When the person is an underwriter, the type of underwriting arrangement, the role of the particular person as an underwriter and the availability of information with respect to the registration; and
- Whether, with respect to a fact or document incorporated by reference, the particular person had any responsibility for the fact or document at the time of the filing from which it was incorporated.

The level of investigation required with respect to the sovereign guarantee would customarily be lower than for a corporate issuer because of the following factors:

- The high credit rating of the sovereign;

- The public availability of public accounts and other information concerning the sovereign;
- The sovereign's debt raising history (*i.e.* the sovereign is seasoned in its own right);
- The short and medium-term tenor of debt securities issued under these programmes (*i.e.* in most cases, the guarantees are only for a maximum of three years).

The amount of due diligence undertaken on sovereign disclosure should depend on the facts and circumstances of the particular sovereign guarantor, the particular disclosure concerning the sovereign and the terms of the offering. Diligence on the corporate issuer should not be affected by the guarantee.

C. Documentation Issues

Sovereigns are unlikely to be willing or even authorised to become parties to underwriting agreements, and as a consequence, underwriters will not be able to obtain the representations and warranties and indemnities customarily provided by guarantors. In the absence of the sovereign being a party to the underwriting agreement, issuer should provide representations, warranties and indemnities concerning the sovereign guarantor. Certain of these representations are necessary in order for counsel to provide their "no registration" opinions.

Underwriters should not expect to receive a comfort letter that covers any country-specific disclosure in the offering document. Governments are traditionally audited by other arms of government rather than external auditors, and direct offerings by sovereign issuers have traditionally not involved a comfort letter. Comfort letters relating to the corporate issuer should not be affected by the guarantee.

Underwriters would expect issuer's counsel to provide an enforceability opinion on the guarantee, which would cover the usual matters such as capacity, and a legal opinion to the effect that the relevant sovereign guarantor is not immune from proceedings brought in respect of the guarantee.

Underwriters should expect to receive a disclosure opinion from their counsel. Disclosure opinions in direct offerings by sovereign issuers ordinarily do not cover statistical information or statistical data included in the disclosure because this information is likely expertised and because of the difficulty that lawyers have in verifying such information.

V. PROSPECTUS DIRECTIVE CONSIDERATIONS

The Prospectus Directive does not apply to non-equity securities issued by a Member State of the EEA or a regional or local authority of a Member State, by public international bodies of which one or more Member States are members, by the European Central Bank or by the central banks of the Member States.[15] It also does not apply to securities unconditionally and irrevocably guaranteed by a Member State or by one of a Member State's regional or local authorities.[16]

On October 14, 2008, the FDIC announced the temporary Liquidity Guarantee Program (the "FDIC Guarantee Programme") to strengthen confidence and encourage liquidity in the U.S. banking system. The FDIC Guarantee Programme will guarantee newly issued senior unsecured debt of eligible institutions, including FDIC-insured banks and thrifts, as well as certain holding companies, and provide full deposit insurance coverage for non-interest bearing deposit transaction accounts in FDIC-insured institutions, regardless of the U.S. dollar amount. The FDIC will guarantee such newly issued senior unsecured debt issued by participating institutions on or after October 14, 2008, and before June 30, 2009.

Non-equity securities issued by a non-EEA country such as the United States or guaranteed by a non-EEA country or an agency or instrumentality of a non-EEA country (such as the FDIC) are not exempt from the provisions of the Prospectus Directive. As a result, the issuance, offer and sale by U.S. financial institutions of debt securities guaranteed by the FDIC to the public in the EEA, or the admission of such securities for trading on a regulated

[15] See Prospectus Directive, Article 1(2)(b).

[16] See Prospectus Directive, Article 1(2)(d).

securities market in the EEA, will be subject to the prospectus preparation and delivery requirements of the Prospectus Directive. Unless the offers and sales of such securities are limited to "qualified investors" within the meaning of the Prospectus Directive or avail themselves of other applicable exemptions thereunder, appropriate sovereign disclosure with respect to the guarantor must be prepared and included in the relevant prospectus. In practice, we expect any such offerings to be conducted pursuant to available exemptions from the prospectus requirements established under the Prospectus Directive.

This publication is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

If you wish to receive more information on the topics covered in this publication, you may contact your regular Shearman & Sterling LLP contact person or any of the following:

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Required Disclosure under Schedule B to the Securities Act

The SEC never adopted specific *forms* for the registration of securities under Schedule B. Schedule B does, however, contain certain requirements with respect to the *contents* of a registration statement. The items listed under Schedule B relate principally to securities issued or guaranteed by foreign sovereigns, and the SEC requires the registration statements to contain a *cross-reference* sheet which attributes each item of Schedule B to the respective heading in the prospectus. However, while Schedule B contains a list with certain disclosure items, such as information relating to the public debt of the issuer, such requirements are not deemed to be exhaustive nor are they deemed to satisfy the general materiality threshold of Rule 408 under the Securities Act. As a result, a prospectus of a foreign sovereign will contain a significant amount of economic, financial and political information about the issuer, largely as a result of an evolving practice of Schedule B issuers, rather than because of an explicit requirement in Schedule B.

The following is a brief description of the type of information required by Schedule B and market practice:

- The names of the guarantor and the names and addresses of the underwriters.
- The specific purpose of the guarantee and the approximate amount to be devoted to such purpose and if funds are to be raised in part from other sources, the amounts thereof and the sources thereof.
- The price at which the proposed security is to be offered.
- The estimated net proceeds to be derived from sale in the United States of the security to be offered.
- Commissions to be paid to the underwriters and other expenses of the offering.
- Country information, including geographic and demographic information, political information, and membership in international organisations.
- Economic information, including descriptions of the main features of the economy in recent years, gross domestic product, description of the labour force, wage and price data and foreign trade data and balance of payment data.
- Financial market information, including information on the administration and function of the central bank, the various types of financial institutions in the country and information on foreign exchange.
- Public finance information, including a description of the budgetary process and tax system, information on receipts, expenditures and the national debt, a description of the amount of funded and floating debt outstanding and to be created by the security being offered and information on whether or not the guarantor has, within the last 20 years, defaulted on the principal or interest of any external security.
- The names and addresses of counsel who have passed upon the legality of the issue.