The Harvard Law School Forum on Corporate Governance and Financial Regulation

Supported by: CSC Corporation Service Company

Creative TruPS Capital Restructurings

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Editor's Note: Edward Herlihy is a partner and co-chairman of the Executive Committee at Wachtell, Lipton, Rosen & Katz. This post is based on a Wachtell Lipton firm memorandum by Mr. Herlihy, Richard K. Kim, Nicholas G. Demmo, Patricia A. Robinson, and Brandon C. Price.

With the phase out of Tier 1 capital treatment for trust preferred securities (TruPS) mandated by Dodd Frank slated to begin January 1, 2013, financial institutions have been active in considering potential strategies to replace outstanding TruPS with other forms of regulatory capital. Last week, Huntington Bancshares completed a novel exchange offer for several specified series of outstanding TruPS. In the offer, Huntington exchanged outstanding floating-rate TruPS for a new series of floating-rate non-cumulative perpetual preferred stock, which – unlike the TruPS – will not lose Tier 1 treatment under Dodd Frank and will also continue to be recognized as a Tier 1 instrument under Basel III.

Huntington's exchange offer involved four different series of TruPS and the offer was tailored to each series, including through the use of additional cash consideration for two of the series and by employing a waterfall of acceptance priority levels among the four series in the event that the offering was oversubscribed. By conducting the exchange as a registered offering rather than relying on the exchange provisions under Section 3(a)(9) of the Securities Act of 1933, Huntington was able to employ a dealer manager to solicit TruPS holders in an effort to maximize participation. Note, however, that while Huntington's exchange offer was completed in the scheduled time frame, the SEC must declare an exchange offer registration statement effective prior to closing, and the SEC review process can risk a delayed closing. Under the securities laws, the offer must be open to all holders and must remain open for at least 20 business days.

A number of financial institutions, including Comerica, KeyCorp, PNC, Wells Fargo and Fifth Third, have also taken action with respect to TruPS, including in certain cases redeeming TruPS under early redemption indenture provisions triggered by the Dodd-Frank regulatory capital treatment changes. (See our July 2010 client memorandum "Potential Opportunities for Issuers of Trust Preferred Securities under the Collins Amendment.") With the start of the three year phase out of Tier 1 capital treatment approaching, financial institutions will continue to explore opportunities to replace TruPS with securities having preferred regulatory capital treatment (and/or a lower cost of capital) and to deploy excess capital to repurchase or redeem TruPS where economically advantageous. Any redemption or replacement strategy requires careful coordination with regulators, financial and legal advisors and consideration of all applicable circumstances, including the investor base of the outstanding TruPS, to appropriately tailor the terms of the transaction and ensure the best opportunity for a successful exchange or redemption. Issuers should also bear in mind applicable corporate and securities law issues, including disclosure obligations, as discussed in our November 2011 client memorandum, "Enforcement Action Underscores Disclosure Obligations with TruPS Capital Restructurings."