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## State Securities Board

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April 9, 2002

Mr. David M. Moore  
Counsel  
State Farm Insurance Companies  
One State Farm Plaza  
Bloomington, Illinois 61710-0001

RE: State Farm Financial Services, F.S.B. (Certificates of Deposit  
Marketed Through Affiliated Third Parties)

Dear Mr. Moore:

This is in response to your letter dated May 15, 2001 and received by this Agency on May 16, 2001, and supplemented by your letter dated January 29, 2002.

Your letters and supplemental materials describe a proposed offering to the public of certificates of deposit ("CDs") issued by State Farm Financial Services, F.S.B. ("State Farm Bank"), a federal savings bank and subsidiary of State Farm Mutual Automobile Insurance Company ("State Farm"). Although the CDs issued by State Farm Bank are FDIC-insured, you noted that, due to the \$100,000 limit on FDIC deposit insurance, the accounts of some State Farm Bank depositors will not be fully insured by the FDIC so that payment in full is not guaranteed.

State Farm Bank plans to provide deposit and loan products and services to customers in Texas primarily through State Farm's exclusive network of independent agents ("Exclusive Agents"). Included among these products will be a fixed rate CD as well as a 5-year variable rate certificate of deposit. The interest rate on the new variable rate CD is tied to the performance of the S&P 500 Stock Index over the period of the CD. If the S&P 500 Stock Index consistently declines during the five-year period, the depositor will still receive his or her principal at maturity.

The State Farm network of Exclusive Agents is primarily composed of individuals who sell State Farm insurance products. You noted that Exclusive Agents are not employees of State Farm but are generally prohibited from selling insurance and financial products issued by non-State Farm organizations. Some Exclusive Agents are registered representatives of State Farm VP Management Corp. ("SFVP"), a Texas registered dealer.

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Exclusive Agents will enter into an agreement with State Farm Bank to market CDs issued by State Farm Bank. Under that agreement, Exclusive Agents will offer State Farm Bank's CDs to their customers and will receive a fee of \$25 from State Farm Bank for each State Farm Bank deposit account that is opened, regardless of the amount of the deposit.

You explained that, as a condition to participation in the marketing of State Farm Bank products, Exclusive Agents must agree to act in accordance with all applicable laws and regulations and all guidelines, procedures, and policies established by State Farm Bank, and must successfully complete training required by State Farm Bank. You represented that State Farm Bank has established a comprehensive compliance plan to seek to ensure that the Exclusive Agents comply with all applicable laws and regulations. As part of the training, Exclusive Agents are issued an "Agent Reference Manual," which they must read and then score 80% or better on a test referred to as a "Certification Assessment." Following passage of this test, the Exclusive Agent and the Exclusive Agent's supervisor must attend live classroom training, lasting approximately one and one-half days. At the completion of the classroom training, the Exclusive Agent signs the sales agreement with State Farm Bank and becomes qualified to sell CDs offered by State Farm Bank.

You noted that Exclusive Agents will provide information and brochures regarding CDs and other products and services offered by State Farm Bank primarily through mailings and through telephone and personal contacts with customers. Exclusive Agents also will display State Farm Bank brochures in their offices. Exclusive Agents will assist customers in completing applications for products of State Farm Bank or, alternatively, may refer customers to a State Farm Bank employee who will assist customers in obtaining the desired product or service. The Exclusive Agents will not accept any cash deposits or make any withdrawals on behalf of State Farm Bank customers. Exclusive Agents will not create a secondary market with respect to the sale of State Farm Bank CDs or otherwise add enhancements or other features to the CDs.

As an initial matter, you have opined that CDs are not securities for the purposes of the Texas Securities Act ("Act"). You cite *Marine Bank v. Weaver*, 455 U.S. 551 (1982) in support of your position. We are not aware of any Texas case embracing the holding of *Marine Bank* for purposes of the Act. Moreover, Section 5.L of the Act and Board Rule 109.17 contain carefully crafted exemptions from the registration requirements for the securities of certain financial institutions under controlled and limited circumstances.

The exemption from securities registration provided by 5.L of the Act is available for the sale by the issuer itself of a security issued by a federal savings and loan association. Board Rule 109.17(b) interprets the phrase "any federal savings and loan association," as used in Section 5.L, to include a federally chartered savings bank, such as State Farm Bank.

The exemption provided by Section 5.M of the Act is available when the guarantee required by that section is full and complete. If sales to be made in Texas could be restricted to persons who would not own, in any capacity, in excess of the \$100,000 amounts for which FDIC insurance coverage is available, the exemption provided by Section 5.M of the Act could be available. However, you have acknowledged that sales in Texas will not be restricted in such a manner so there may be instances where the CDs will not be fully insured by the FDIC. Thus, the exemption provided by Section 5.M does not appear to be available for the offering of the CDs in these circumstances.

Section 4.C of the Act defines "dealer" to include the following:

... every person or company ... who engages in this state, either for all or part of his or its time, directly or through an agent, in selling, offering for sale or delivery or soliciting subscriptions to or orders for, or undertaking to dispose of, or to invite offers for any security or securities and every person or company who deals in any other manner in any security or securities within this state. ...

Please note that the Texas courts have broadly construed this definition and determined that a person is "selling" securities if he or she is any link in the "chain of sale." See *Brown v. Cole*, 155 Tex. 624, 291 S.W.2d 704 (1956). The Act goes on to define "agent" to include "every person or company employed or appointed or authorized by a dealer to sell, offer for sale or delivery, or solicit subscriptions to or orders for, or deal in any other manner, in securities within this state, whether by direct act or through subagents ..."

Based on the foregoing understanding, the exemption provided by Section 5.L of the Act is available for the CDs issued by State Farm Bank and for the personnel of State Farm Bank assisting in the offer and sale of the CDs. The staff of the State Securities Board respectfully declines to recommend a no action position in regard to State Farm, SFVP, and the Exclusive Agents (collectively, the "State Farm Bank Affiliates"). The State Farm Bank Affiliates meet the definitions of "dealer" or "agent" contained in the Act, and would be required to register as such.

Please note that, due to the limits placed on the activities of the Exclusive Agents of the State Farm Bank Affiliates, the Securities Commissioner will consider whether to waive the requirement of an examination over general securities law principles if you wish to make such a request in conjunction with the application for registration. The proper way to request an examination waiver is to provide detailed information regarding the nature of the activities of the Exclusive Agents, submit such information with the application, and request waiver of the examination requirement based upon the limited nature of the securities-related activities. It is acceptable to request a blanket waiver to cover all State Farm Bank Affiliates which register or will register in the future as long as there is a representation in the request to the effect that the activities of all affected Exclusive Agents will be

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the same. Please keep in mind that if, at some point, the activities performed by the State Farm Bank Affiliates or the Exclusive Agents were to extend beyond that described above, then it may become necessary for those individuals to complete additional examination requirements.

Please note that this Agency has not made an independent investigation of the facts, but has relied solely on the information you have provided. If this information is incorrect or changes substantially, the staff would reconsider the matter and the opinion stated above would be void.

Further, this Agency does not grant nor confer an exemption. Its availability depends entirely on full compliance with the language of the exemption. If a dispute arises about availability of an exemption, the burden of proof falls on the party claiming the exemption.

Finally, the opinions expressed by this Agency are not binding on civil litigants in future proceedings.

I trust this letter answers your inquiry. Please feel free to write us if you need further information.

Very truly yours,

DENISE VOIGT CRAWFORD  
Securities Commissioner

David Weaver  
General Counsel

DW/ms