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Second Circuit Holds That the Syndicated Term Loans in Kirschner Are Not Securities

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On August 24, 2023, the Second Circuit Court of Appeals issued its much-anticipated decision in *Kirschner v. JP Morgan Chase Bank*, holding that the syndicate term loans at issue were not securities. As noted in our earlier blog post, the SEC declined the court's request to file an *amicus* brief, forgoing the opportunity to provide its views on the issue and influence the outcome of the appeal.[1]

In affirming the district court's dismissal of the plaintiff's state-law securities claims, the court applied the four-factor "family resemblance" test previously established by the Second Circuit and later adopted by the U.S. Supreme Court in *Reves v. Ernst & Young*. While the court recognized that the lenders' motivation was investment given their expectation of profit from their purchase of the notes (a factor weighing in favor of the notes being a securities), the court was persuaded by the other three factors under *Reves* that weighed against concluding that the notes were securities.

- First, in examining the plan of distribution, the court found that the notes were not offered and sold to a broad segment of the public. While there was a secondary market, the notes were generally unavailable to the general public by virtue of restrictions on assignments of the notes.
- Second, in assessing the reasonable expectations of the public, the court found that the lenders were sophisticated and experienced institutional entities with ample notice that the notes were not securities.
- Finally, in evaluating the presence of other risk-reducing factors, the court concluded that the protection afforded by the application of the securities laws was unnecessary. The court relied on the notes being secured by collateral and the bank regulators' issuance of specific policy guidance addressing syndicated loans.

The decision itself is not all that surprising, especially given the precedent established by Second Circuit over thirty years ago in *Banco Espanol de Credito v. Nat. Bank*. But the decision does illustrate how the determination of whether a note will be deemed a security ultimately is a facts and circumstances test and that under different circumstances, a particular debt instrument could be held to be a security.

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[1] The Second Circuit noted in a footnote the SEC's decision not to file a brief "[a]fter receiving several extensions of time to file its response to our invitation to provide its views on this question . . . ." Id. at 37 n. 117.

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