FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 82-127
October 7, 1982

REGULATION T

CREDIT BY BROKERS AND DEALERS

Proposed Amendment

TO ALL MEMBER BANKS,
OTHER CREDITORS, AND OTHERS CONCERNED
IN THE ELEVENTH FEDERAL RESERVE DISTRICT:

The Board of Governors of the Federal Reserve System is proposing for public comment an amendment to Regulation T that would specify the characteristics of private mortgage-backed securities that may be used as collateral for margin credit at securities brokers. Comments on the proposed amendment should be received on or before October 29, 1982.

Enclosed are copies of the Board's press release and the material submitted to the Federal Register detailing the proposed changes of the Regulation.

Interested persons are invited to submit comments to the Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. Please refer to Docket No. R-0423 when submitting comments.

Questions concerning the proposed amendment should be directed to this Bank's Legal Department, Extension 6171.

Additional copies of this circular may be obtained from the Department of Communications, Financial and Community Affairs, Extension 6289.

Sincerely yours,

William H. Wallace

William H. Wallace
First Vice President

Enclosures

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FEDERAL RESERVE press release

For immediate release

September 23, 1982

The Federal Reserve Board today proposed, for public comment, an amendment to Regulation T that would specify the characteristics of private mortgage-backed securities that may be used as collateral for margin credit at securities brokers.

Comment should be received on or before October 29, 1982.

The proposed rule would amend the definition of OTC margin bonds to specify that private mortgage pass-through certificates may be bought on margin at a "good faith" loan value under the same general criteria established for corporate bonds.

However, unlike a corporate issue, the principal balance of a private mortgage-backed security declines each month as mortgages backing the security are amortized or prepaid. Consequently, the proposed amendment would require (1) an original minimum issue of $25,000,000 (rather than an outstanding principal amount at the time credit is extended) that may be sold in separate series, (2) current filings with the Securities and Exchange Commission, and (3) the passing through of mortgage interest and principal payments by the servicing agent according to the terms of the offering.

The Board specifically requests comment as to whether the $25,000,000 minimum initial size is an appropriate criterion to establish adequate marketability of the security for margin account purposes. In addition, the Board requests views as to the likelihood that a broker would liquidate these securities to meet margin calls when there are other types of securities in the customer's account with that broker.

The Board's notice is attached.

Attachment

Federal Reserve System

Regulation T

(12 CFR 220)

[Docket No. R - 0423]

CREDIT BY BROKERS AND DEALERS

Private Mortgage Pass-through Securities as OTC Margin Bonds

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed Rule.

SUMMARY: The Board is proposing for public comment an amendment to Regulation T that will specify the characteristics of "private" mortgage pass-through securities (i.e., not guaranteed by agencies of the United States government) that may be used as collateral for margin credit at securities brokerage firms. The existing definition of "OTC margin bond" in Regulation T will be expanded to cover these instruments. At present, any "OTC margin bond" is eligible for credit on a "good faith" basis. The proposed criteria for inclusion of a private mortgage pass-through security in the definition of "OTC margin bond" differ from the criteria in the existing definition because of the nature of the mortgage pass-through security. Unlike a typical corporate bond, the principal balance of this security declines each month as mortgages backing the security are amortized or prepaid. The proposed criteria, therefore, will require (1) an original issue of $25,000,000 (rather than an outstanding principal amount at the time credit is extended) that may be sold in separate series, (2) current filings with the Securities and Exchange Commission, and (3) the passing through of mortgage interest and principal payments by the servicing agent according to the terms of the offering. The Board specifically requests comment as to whether the $25,000,000 minimum initial size is an appropriate criterion to establish adequate marketability of the security for margin account purposes. In addition, the Board requests views as to the likelihood that a broker would liquidate these securities to meet margin calls when there are other types of securities in the customer's account with that broker.

DATE: Comments should be received on or before October 29, 1982.

ADDRESS: Comments, which should refer to Docket No. R-0423, may be mailed to the Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551 or delivered to Room B-2223 between 8:45 a.m. and 5:15 p.m. Comments received may also be inspected at Room B-1122 between 8:45 a.m. and 5:15 p.m.

FOR FURTHER INFORMATION CONTACT: Laura Homer or Robert Lord, Division of Banking Supervision and Regulation (202) 452-2781 or David Seiders, Division of Research and Statistics, (202) 452-2694, at the Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

INITIAL REGULATORY FLEXIBILITY ANALYSIS:

The Board believes there will be no significant economic impact on a substantial number of small entities if this proposed rule is adopted.

LIST OF SUBJECTS IN 12 CFR 220

Banks, Banking; Brokers; Credit; Federal Reserve System; Margin; Margin Requirements; Reporting Requirements; Securities.

Pursuant to sections 7 and 23 of the Securities Exchange Act of 1934, as amended (15 U.S.C. 78g and w), the Board proposes to amend Regulation T (12 CFR 220) as set forth below:

§ 220.2 -- Definitions

* * * * *

(i) The term "OTC margin bond" means (1) a debt security not traded on a national securities exchange which meets all of the following requirements:

(i) At the time of the extension of credit, a principal amount of not less than $25,000,000 of the issue is outstanding.

(ii) The issue was registered under section 5 of the Securities Act of 1933 and the issuer either files periodic reports pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934 or is an insurance company which meets all of the conditions specified in section 12(g)(2)(G) of the Act.

(iii) At the time of the extension of credit, the creditor has a reasonable basis for believing that the issuer is not in default on interest or principal payments; or

(2) a private mortgage pass-through security (not guaranteed by an agency of the U.S. government) meeting all of the following requirements:

(i) an aggregate principal amount of not less than $25,000,000 (which may be issued in series) was issued pursuant to a registration statement filed with the Securities and Exchange Commission under section 5 of the Securities Act of 1933.

(ii) Current reports relating to the issue have been filed with the Securities and Exchange Commission.

(iii) At the time of the credit extension, the creditor has a reasonable basis for believing that mortgage interest and principal payments are being passed through and that the servicing agent is meeting all the obligations required under the terms of the offering.

By order of the Board of Governors of the Federal Reserve System, September 22, 1982.

(signed)
James McAfee
Associate Secretary of the Board

[SEAL]