

FEDERAL RESERVE BANK
OF NEW YORK

ATG-295

February 19, 1969

Proposed Amendment of Regulation T

To Brokers, Dealers, and Members of National Securities Exchanges in the Second Federal Reserve District:

Printed below is an excerpt from the *Federal Register* of February 15, containing the text of the proposed amendment of margin Regulation T of the Board of Governors of the Federal Reserve System, which would extend the regulation to cover certain securities that are not registered on a national securities exchange.

Comments on the proposed amendment may be submitted by March 17, 1969 and should be sent to our Bank Examinations Department. Additional copies of the texts of the proposed amendments of this regulation and of the Board's margin Regulations G and U will be furnished upon request.

ALFRED HAYES,
President.

[12 CFR Part 220]

[Reg. T]

NATIONAL SECURITIES EXCHANGES

Credit by Brokers, Dealers, and
Members

Pursuant to the authority contained in the Securities Exchange Act of 1934 (15 U.S.C. 78g), as amended by Act of July 29, 1968 (Public Law 90-437; 82 Stat. 452), the Board of Governors of the Federal Reserve System is considering amending Part 220 (Regulation T) as set forth below in order to regulate the amount of credit that may be extended with respect to certain securities that are not registered on a national securities exchange.

Public Law 90-437 broadens the Board's authority over stock market credit to cover "over-the-counter" (OTC) stocks. The legislation leaves to the Board the timing and selection of criteria for the implementation of OTC margin requirements.

The proposed amendments to Regulation T are principally designed to include in the regulation criteria under which the Board will select OTC stocks which would be subject to the margin and other requirements of the regulation. Initially, such "OTC margin stock" would be stock, not traded on a national securities exchange, which the Board has determined to have the degree of national investor interest, the depth and breadth of market, the availability of information respecting such stocks and their issuers, and the character and permanence of the issuers, to warrant treatment similar to stocks that are registered on such exchanges.

Under the proposed regulatory framework, any broker/dealer would be permitted to lend his customers the amount the regulation permits (currently 20 percent) against OTC margin stocks, but he could not borrow more than this against such stocks from a bank (with certain exceptions set forth in Part 221—Regulation U) or other lender unless he was rehypothecating his customers' securities or was registered as an OTC market-maker in the stock to be pledged, and such stock was being used in the performance of his function as such a market-maker.

In a related change, the definition of "creditor" would be broadened to cover any broker or dealer, whether or not a member of a national securities exchange

or transacting a business in securities through the medium of such a member. A conforming change would be made in the special omnibus account provision (§ 220.4(b)) so that exempt credit, presently extended on their customers' securities to brokers or dealers who merely undertake to observe the requirements of Regulation T, would be limited in the future to those who are prepared to certify that they are actually subject to this part. Most firms borrowing under § 220.4(b) would not be affected. However, in the case of credit extended under this section to persons or firms who are not prepared to certify that they are actually subject to this part (regulation T), no substitutions of collateral would be permitted after 90 days from the adoption of this proposal; and such credit would be required to be extinguished within one year after that date, if the proposals are adopted.

The proposal would also introduce to the regulation the term "regulated security" which would encompass registered securities and OTC margin stock. Accordingly, regulated equity securities would be treated throughout this part as registered equity securities now are, with corresponding conforming changes as necessary or appropriate.

The proposed amendments would also provide for a committee of a national securities association to extend the 5-day period, within which the required deposit must be made in connection with transactions in the general (margin) account, corresponding to the procedure presently followed by a committee of a national securities exchange.

It is also proposed that statements be obtained on a new form (Federal Reserve Form T-4) in connection with "non-purpose" extensions of credit collateralized by regulated securities.

In addition, the proposal would clarify that for the purpose of Part 220 it is immaterial whether a debt security is convertible, with or without consideration, presently or in the future, into a regulated stock.

This notice is published pursuant to section 553(b) of title 5, United States Code, and § 262.2(a) of the rules of procedure of the Board of Governors of the Federal Reserve System (12 CFR 262.2(a)).

To aid in the consideration of this matter by the Board, interested persons are invited to submit, in writing, relevant

data, views, or arguments. Such material should be submitted to any Federal Reserve Bank, to be received not later than March 17, 1969. Under the Board's rules regarding availability of information (12 CFR Part 261), such materials will be made available for inspection and copying to any person upon request unless the person submitting the material requests that it be considered confidential.

Dated at Washington, D.C., this 10th day of February 1969.

By order of the Board of Governors.

[SEAL] ROBERT P. FORRESTAL,
Assistant Secretary.

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AUTHORITY: The provisions of this Part 220 issued under secs. 7 and 8(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78g, 78h (a)) as amended by Public Law 90-437 (82 Stat. 452).

§ 220.1 Scope of part.

This part is issued by the Board of Governors of the Federal Reserve System (hereinafter called the "Board") pursuant to the Securities Exchange Act of 1934 (called the "Act" in this part), particularly sections 7 and 8(a) thereof (15 U.S.C. 78g, 78h(a), as amended), and applies to every dealer, including every member of a national securities exchange.

§ 220.2 Definitions.

For the purposes of this part, unless the context otherwise requires:

(a) The terms "person," "member," "broker," "dealer," "buy," "purchase," "sale," "sell," "security," "equity security," and "bank" have the meanings given them in section 3(a) of the Act (15 U.S.C. 78c(a)).

(b) The term "creditor" means any broker or dealer including every member of a national securities exchange.

(c) The term "customer" includes any person, or any group of persons acting jointly, (1) to or for whom a creditor is extending or maintaining any credit, or (2) who, in accordance with the ordinary usage of the trade, would be considered a customer of the creditor. It includes, in case the creditor is a firm, any partner in the firm who would be considered

a customer of the firm if he were not a partner, and includes any joint adventure in which a creditor participates and which would be considered a customer of the creditor if the creditor were not a participant.

(d) The term "registered security" means any security which (1) is registered on a national securities exchange; or (2) in consequence of its having unlisted trading privileges on a national securities exchange is deemed, under the provisions of section 12(f) of the Act (15 U.S.C. 781), to be registered on a national securities exchange; or (3) is exempted by the Securities and Exchange Commission from the operation of section 7(c) (2) of the Act (15 U.S.C. 78g(c) (2)) only to the extent necessary to render lawful any direct or indirect extension or maintenance of credit on such security or any direct or indirect arrangement therefor which would not have been unlawful if such security had been a security (other than an exempted security) registered on a national securities exchange.

(e) (1) The term "OTC margin stock" means stock, not traded on a national securities exchange, which the Board of Governors of the Federal Reserve System has determined to have the degree of national investor interest, the depth and breadth of market, the availability of information respecting the stock and its issuer, and the character and permanence of the issuer to warrant such treatment.

(2) The Board will from time to time publish a list of OTC margin stock as to which the Board has made the determinations described in subparagraph (1) of this paragraph (e). Except as provided in subparagraph (4) of this paragraph (e), such stocks shall meet the requirements that:

(i) The stock is subject to registration under section 12(g) (1) of the Securities Exchange Act of 1934 (15 U.S.C. 781(g) (1)), or if issued by an insurance company subject to section 12(g) (2) (G) (15 U.S.C. 781(g) (2) (G)), the issuer had at least \$1 million of capital and surplus,

(ii) Five or more dealers, stand willing to, and do in fact, make a market in such stock including making regularly published bona fide bids and offers for such stock for their own accounts, or the stock is registered on a securities exchange that is exempted by the Securities and Exchange Commission from registration as a national securities exchange pursuant to section 5 of the Act (15 U.S.C. 78e),

(iii) There are 1,500 or more holders of record of the stock who are not officers, directors, or beneficial owners of 10 percent or more of the stock,

(iv) The issuer, or a predecessor in interest, has been in existence for at least 3 years,

(v) The stock has been publicly traded for at least 6 months, and

(vi) Daily quotations for both bid and asked prices for the stock are continuously available to the general public;

and shall meet three of the four additional requirements that:

(vii) There are 500,000 or more shares of such stock outstanding in addition to shares held beneficially by officers, directors, or beneficial owners of more than 10 percent of the stock,

(viii) The shares described in subdivision (vii) of this subparagraph have a market value in the aggregate of at least \$10 million,

(ix) The minimum average bid price of such stock, as determined by the Board in the latest month, is at least \$10 per share, and

(x) The issuer had at least \$5 million of capital, surplus and undivided profits.

(3) The Board shall from time to time remove from the list described in subparagraph (2) of this paragraph (e) stocks that cease to:

(i) Exist or for which the issuer ceases to exist, or

(ii) Meet substantially, the provisions of subparagraph (1) of this paragraph (e).

(4) The foregoing notwithstanding, the Board may, upon its own initiative, or upon application by any interested party, omit or remove any stock that is not traded on a national securities exchange from or add any such stock to such list of OTC margin stocks if in the judgment of the Board, such action is necessary or appropriate in the public interest.

(5) It shall be unlawful for any creditor to make, or cause to be made, any representation to the effect that the inclusion of a security on such list of OTC margin stocks is evidence that the Board or the Securities and Exchange Commission has in any way passed upon the merits of, or given approval to, such security or any transaction therein. Any statement, advertisement, or other similar communication containing a reference to the Board in connection with such stocks or such list shall constitute such an unlawful representation.

(f) The term "regulated security" means any registered security or OTC margin stock.

(g) The term "exempted security" has the meaning given it in section 3(a) of the Act (15 U.S.C. 78c(a) (12)), except that the term does not include a security which is exempted by the Securities and Exchange Commission from the operation of section 7(c) (2) of the Act (15 U.S.C. 78g(c) (2)) only to the extent described in paragraph (d) (3) of this section.

(h) The term "non-equity security" means any security other than an equity security or an exempted security.

§ 220.3 General accounts.

(a) *Contents of general account.* All financial relations between a creditor and a customer, whether recorded in one record or in more than one record, shall be included in and be deemed to be part of the customer's general account with the creditor, except that the relations which § 220.4 permits to be included in any special account provided for by that section may be included in the appropriate special account, and all transactions in commodities, and, except to the extent provided in paragraph (b) (2)

of § 220.3, all transactions in nonequity securities, exempted securities, and in other securities having no loan value in a general account under the provisions of §§ 220.3(c) and 220.8 (the Supplement to Regulation T) (except unissued securities, short sales and purchases to cover short sales, securities positions to offset short sales, and contracts involving an endorsement or guarantee of any put, call, or other option), shall be included in the appropriate special account provided for by § 220.4. During any period when such § 220.8 specifies that regulated equity securities shall have no loan value in a general account or special convertible debt security account subject to § 221.4(j), any transaction consisting of a purchase of a security other than a purchase of a security to reduce or close out a short position shall be effected in the special cash account provided for by § 220.4(c) or in some other appropriate special account provided for by § 220.4.

(b) *General rule.* (1) A creditor shall not effect for or with any customer in a general account, special bond account subject to § 220.4(i), or special convertible debt security account (sometimes referred to herein as "special convertible security account") subject to § 220.4(j) any transaction which, in combination with the other transactions effected in such account on the same day, creates an excess of the adjusted debit balance of such account over the maximum loan value of the securities in such account, or increases any such excess, unless in connection therewith the creditor obtains, as promptly as possible and in any event before the expiration of 5 full business days following the date of such transaction, the deposit into such account of cash or securities in such amount that the cash deposited plus the loan value of the securities deposited equals or exceeds the excess so created or the increase so caused.

(2) Except as permitted in this subparagraph, no withdrawal of cash or regulated or exempted securities shall be permissible if the adjusted debit balance of the account (whether the general account, the special bond account subject to § 220.4(i) or the special convertible security account subject to § 220.4(j)) would exceed the maximum loan value of the securities in such account after such withdrawal. The exceptions are available only in the event no cash or securities need to be deposited in such account in connection with a transaction on a previous day and none would need to be deposited thereafter in connection with any withdrawal of cash or securities on the current day. The permissible exceptions are (i) registered nonequity securities or exempted securities held in the general account on March 11, 1968, and continuously thereafter may be withdrawn upon the deposit in the account of cash (or regulated equity securities counted at their maximum loan value) at least equal to the "retention requirement" of such withdrawn securities, or (ii) except as provided in subdivision (i) of this subparagraph, securities having loan value in the general

account, the special bond account subject to § 220.4(i), or the special convertible security account subject to § 220.4(j) may be withdrawn upon the deposit in such account of cash or securities having loan value in such account counted at the maximum loan value at least equal to the "retention requirement" of those securities, or (iii) cash may be withdrawn upon the deposit in the general account, the special bond account subject to § 220.4(i), or the special convertible security account subject to § 220.4(j) of securities having a maximum loan value in such account at least equal to the amount of cash withdrawn, or (iv) upon the sale (other than the short sale) of securities having loan value in the general account, special bond account subject to § 220.4(i) or special convertible security account subject to § 220.4(j) there may be withdrawn in cash an amount equal to the difference between the current market value of the securities sold and the "retention requirement" of such securities, or (v) upon the sale (other than the short sale) of a registered nonequity security or an exempted security that was held in the general account on March 11, 1968, and continuously thereafter there may be withdrawn in cash an amount equal to the difference between the current market value of the securities sold and the "retention requirement" of those securities as prescribed in § 220.8 (the Supplement to Regulation T).

(3) Rules for computing the maximum loan value of the securities in a general account, special bond account subject to § 220.4(i) or special convertible security account subject to § 220.4(j) and the adjusted debit balance of such account are provided in paragraphs (c) and (d) of this section, and certain modifications of and exceptions to the general rule stated in this paragraph are provided in the subsequent paragraphs of this section and in § 220.6.

(c) *Maximum loan value and current market value.* (1) The maximum loan value of the securities in a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j) is the sum of the maximum loan values of the individual securities in such account, including securities (other than unissued securities) bought for such account but not yet debited thereto, but excluding securities sold for such account whether or not payment has been credited thereto.

(2) Except as otherwise provided in this paragraph, the maximum loan value of a security in a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j) shall be such maximum loan value as the Board shall prescribe from time to time in § 220.8 (the Supplement to Regulation T). No collateral other than an exempted security or a registered nonequity security held in such account on March 11, 1968, and continuously thereafter, or regulated equity security shall have any loan value in a general account except that a regis-

tered equity security eligible for a special convertible security account pursuant to § 220.4(j) shall have loan value in a general account only if held in the account on March 11, 1968, and continuously thereafter.

(3) A warrant or certificate which evidences only a right to subscribe to or otherwise acquire any security and which expires within 90 days of issuance shall have no loan value in a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j); but, if the account contains the security to the holder of which such warrant or certificate has been issued and such warrant or certificate is held in an appropriate account maintained by the creditor for the customer the current market value of such security (if such security is a regulated security) shall, for the purpose of calculating its maximum loan value, be increased by the current market value of such warrant or certificate.

(4) For the current market value of a security throughout the day of its purchase or sale, the creditor shall use its total cost or the net proceeds of its sale, as the case may be, and at any other time shall use the closing sale price of the security on the preceding business day as shown by any regularly published reporting or quotation service. In the absence of any such closing sale price, the creditor may use any reasonable estimate of the market value of such security as of the close of business on such preceding business day.

(d) *Adjusted debit balance.* For the purpose of this part, the adjusted debit balance of a general account, special bond account subject to § 220.4(i) or special convertible security account subject to § 220.4(j) shall be calculated by taking the sum of the following items:

(1) The net debit balance, if any, of such account;

(2) The total cost of any securities (other than unissued securities) bought for such account but not yet debited thereto;

(3) The current market value of any securities (other than unissued securities) sold short in the general account plus, for each security (other than an exempted security), such amount as the Board shall prescribe from time to time in § 220.8 (the Supplement to Regulation T) as the margin required for such short sales, except that such amount so prescribed in such § 220.8 need not be included when there are held in the general account the same securities or securities exchangeable or convertible within 90 calendar days, without restriction other than the payment of money, into such securities sold short;

(4) The amount of margin specified by paragraph (h) of this section for every net commitment in such account in unissued securities, plus all unrealized losses on each commitment in unissued securities and minus all unrealized gains (not exceeding the required margin) on each commitment in unissued securities; and

(5) The amount of any margin customarily required by the creditor in con-

nection with his endorsement or guarantee of any put, call or other option; and deducting therefrom the sum of the following items:

(6) The net credit balance, if any, of such account; and

(7) The net proceeds of sale of any securities (other than unissued securities) sold for such account but for which payment has not yet been credited thereto.

In case such account is the account of a partner of the creditor or the account of a joint venture in which the creditor participates, the adjusted debit balance shall be computed according to the foregoing rule and the supplementary rules prescribed in § 220.6 (a) and (b).

(e) *Liquidation in lieu of deposit.*¹ In any case in which the deposit required by paragraph (b) of this section, or any portion thereof, is not obtained by the creditor within the 5-day period specified therein, regulated nonexempted securities shall be sold (or, to the extent that there are insufficient regulated nonexempted securities in the general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j) other liquidating transactions shall be effected in such account), prior to the expiration of such 5-day period, in such amount that the resulting decrease in the adjusted debit balance of such account exceeds, by an amount at least as great as such required deposit or the undeposited portion thereof, the "retention requirement" of any regulated or exempted securities sold: *Provided*, That a creditor is not required to sell securities or to effect other liquidating transactions specified by this paragraph in an amount greater than necessary to eliminate the excess of the adjusted debit balance of such account over the maximum loan value of the securities remaining in such account after such liquidation.

(f) *Extensions of time.* In exceptional cases, the 5-day period specified in paragraph (b) of this section may, on application of the creditor, be extended for one or more limited periods commensurate with the circumstances (1) by any regularly constituted committee of a national securities exchange having jurisdiction over the business conduct of its members, of which exchange the creditor is a member or through which his transactions are effected, or (2) in instances where the procedure described above is not readily available or appropriate, by a committee of a national securities association: *Provided*, That such committee is satisfied that the creditor is acting in good faith in making the application and that the circumstances are in fact exceptional and warrant such action.

¹ This requirement relates to the action to be taken when a customer fails to make the deposit required by § 220.3(b), and it is not intended to countenance on the part of customers the practice commonly known as "free-riding", to prevent which the principal national securities exchanges have adopted certain rules. See the rules of such exchanges and § 220.7(e).

(g) *Transactions on given day.* For the purposes of paragraph (b) of this section, the question of whether or not an excess of the adjusted debit balance of a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j) over the maximum loan value of the securities in such account is created or increased on a given day shall be determined on the basis of all the transactions in the account on such day exclusive of any deposit of cash, deposit of securities, covering transaction or other liquidation that has been effected on such day, pursuant to the requirement of paragraphs (b) or (e) of this section, in connection with a transaction on a previous day. In any case in which an excess so created, or increase so caused, by transactions on a given day does not exceed \$100, the creditor need not obtain the deposit specified therein in subparagraph (b) (1) of this section. Any transaction which serves to meet the requirements of paragraph (e) of this section or otherwise serves to permit any offsetting transaction in an account shall, to that extent, be unavailable to permit any other transaction in such account. For the purposes of this part (Regulation T), if a security has maximum loan value under paragraph (c) (1) of this section in a general account, a sale of the same security (even though not the same certificate) in such account shall be deemed to be a long sale and shall not be deemed to be or treated as a short sale.

(h) *Unissued securities.* (1) The amount to be included in the adjusted debit balance of a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j) as the margin required for a net long commitment in unissued securities shall be the current market value of the net amount of unissued securities long minus the maximum loan value which such net amount of securities would have if they were issued regulated securities held in such account; and the amount to be so included as the margin required for a net short commitment in unissued securities shall be the amount which would be required as margin for the net amount of unissued securities short if such securities were issued securities and were sold short in such account: *Provided*, That no amount need be included as margin for a net short commitment in unissued securities when there are held in such account securities in respect of which the unissued securities are to be issued, nor for any net position in unissued securities that are exempted securities.

(2) Whenever a creditor, pursuant to a purchase of an unissued security for a customer, receives an issued security which is not a regulated or exempted security, the creditor shall treat any payment by him for such issued security as a transaction (other than a withdrawal) which increases the adjusted debit balance of a general account, special bond account subject to § 220.4(i), or special convertible security account subject to

§ 220.4(j) by the amount of the payment minus the amount required to be included in the adjusted debit balance of such account, at the time of and in connection with the purchase of the unissued security, as the margin required for such purchase.

§ 220.4 Special accounts.

(a) *General rule.* (1) Pursuant to this section, a creditor may establish for any customer one or more special accounts.

(2) Each such special account shall be recorded separately and shall be confined to the transactions and relations specifically authorized for such account by the appropriate paragraph of this section and to transactions and relations incidental to those specifically authorized. An adequate record shall be maintained showing for each such account the full details of all transactions in the account.

(3) A special account established pursuant to this section shall not be used in any way for the purpose of evading or circumventing any of the provisions of this part. If a customer has with a creditor both a general account and one or more such special accounts, the creditor shall treat each such special account as if the customer had with the creditor no general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j).

(4) The only other conditions to which transactions in such special accounts shall be subject under the provisions of this part shall be such conditions as are specified in the appropriate paragraph of this section and in § 220.2, § 220.6, § 220.7, or § 220.8.

(b) *Special omnibus account.* In a special omnibus account, a member of a national securities exchange may effect and finance transactions for a broker or dealer from whom the member accepts in good faith¹ a signed statement to the effect that he is subject to the provisions of this part and from whom the member receives (1) written notice, pursuant to a rule of the Securities and Exchange Commission concerning the hypothecation of customers' securities by brokers or dealers (Rule 8c-1 (17 CFR § 240.8c-1) or Rule 15c2-1 (17 CFR § 240.15c2-1)), to the effect that all securities carried in the account will be carried for the account of the customers of the broker or dealer and (2) written notice that any short sales effected in the account will be short sales made in behalf of the customers of the broker or dealer other than his partners.

(c) *Special cash account.* (1) In a special cash account, a creditor may effect for or with any customer bona fide cash transactions in securities in which the creditor may:

(i) Purchase any security for, or sell any security to, any customer, provided funds sufficient for the purpose are already held in the account or the purchase or sale is in reliance upon an agreement accepted by the creditor in good faith that the customer will promptly make

full cash payment for the security and that the customer does not contemplate selling the security prior to making such payment.

(ii) Sell any security for, or purchase any security from, any customer, provided the security is held in the account or the creditor is informed that the customer or his principal owns the security and the purchase or sale is in reliance upon an agreement accepted by the creditor in good faith that the security is to be promptly deposited in the account.

(2) In case a customer purchases a security (other than an exempted security) in the special cash account and does not make full cash payment for the security within 7 days after the date on which the security is so purchased, the creditor shall, except as provided in subparagraphs (3)-(7) of this paragraph, promptly cancel or otherwise liquidate the transaction or the unsettled portion thereof.

(3) If the security when so purchased is an unissued security, the period applicable to the transaction under subparagraph (2) of this paragraph shall be 7 days after the date on which the security is made available by the issuer for delivery to purchasers. If the security when so purchased is a "when distributed" security which is to be distributed in accordance with a published plan, the period applicable to the transaction under subparagraph (2) of this paragraph shall be 7 days after the date on which the security is so distributed. If the security when so purchased is a new security issued or to be issued for the purpose of refunding outstanding securities which mature, or are to be payable upon presentation for redemption, within 35 days of the date on which the new security is made available by the issuer for delivery to purchasers, the period applicable to the transaction under subparagraph (2) of this paragraph shall be 7 days after such maturity or payment date: *Provided*, That this sentence shall apply only to the payment of that portion of the purchase price that does not exceed 103 percent of the amount that will be payable to the purchaser of the new security upon such maturity of, or payment for, securities owned by him at the time of the purchase.

(4) If any shipment of securities is incidental to the consummation of the transaction, the period applicable to the transaction under subparagraph (2) of this paragraph shall be deemed to be extended by the number of days required for all such shipments, but not by more than 7 days.

(5) If the creditor, acting in good faith in accordance with subparagraph (1) of this paragraph, purchases a security for a customer, or sells a security to a customer, with the understanding that he is to deliver the security promptly to the customer, and the full cash payment to be made promptly by the customer is to be made against such delivery, the creditor may at his option treat the transaction as one to which the period applicable under subparagraph

¹ As defined in § 220.7(c).

(2) of this paragraph is not the 7 days therein specified but 35 days after the date of such purchase or sale.

(6) If an appropriate committee of a national securities exchange or a national securities association is satisfied that the creditor is acting in good faith in making the application, that the application relates to a bona fide cash transaction, and that exceptional circumstances warrant such action, such committee, on application of the creditor, may (1) extend any period specified in subparagraphs (2), (3), (4), or (5) of this paragraph for one or more limited periods commensurate with the circumstances, or (1), in case a security purchased by the customer in the special cash account is a regulated or exempted security, authorize transfer of the transaction to a general account, special bond account subject to § 220.4(i), special convertible security account subject to § 220.4(j), or special omnibus account and completion of the transaction pursuant to the provisions of this part relating to such an account.

(7) The 7-day periods specified in this paragraph refer to 7 full business days. The 35-day period and the 90-day period specified in this paragraph refer to calendar days, but if the last day of any such period is a Saturday, Sunday, or holiday, such period shall be considered to end on the next full business day. For the purposes of this paragraph, a creditor may, at his option, disregard any sum due by the customer not exceeding \$100.

(8) Unless funds sufficient for the purpose are already in the account, no security other than an exempted security shall be purchased for, or sold to, any customer in a special cash account with the creditor if any security other than an exempted security has been purchased by such customer in such an account during the preceding 90 days, and then, for any reason whatever, without having been previously paid for in full by the customer, the security has been sold in the account or delivered out to any broker or dealer: *Provided*, That an appropriate committee of a national securities exchange or a national securities association, on application of the creditor, may authorize the creditor to disregard for the purposes of this subparagraph any given instance of the type therein described if the committee is satisfied that both creditor and customer are acting in good faith and that circumstances warrant such authorization. For the purposes of this subparagraph, the cancellation of a transaction, otherwise than to correct an error, shall be deemed to constitute a sale. The creditor may disregard for the purposes of this subparagraph a sale without prior payment provided full cash payment is received within the period described by subparagraph (2) of this paragraph and the customer has not withdrawn the proceeds of sale on or before the day on which such payment (and also final payment of any check received in that connection) is received. The creditor may so disregard a delivery of a security to another broker or dealer provided such delivery was for deposit

into a special cash account which the latter broker or dealer maintains for the same customer and in which account there are already sufficient funds to pay for the security so purchased; and for the purpose of determining in that connection the status of a customer's account at another broker or dealer, a creditor may rely upon a written statement which he accepts in good faith from such other broker or dealer.

(d) *Special arbitrage account.* In a special arbitrage account, a member of a national securities exchange may effect and finance for any customer bona fide arbitrage transactions in securities. For the purposes of this paragraph, the term "arbitrage" means (1) a purchase or sale of a security in one market together with an offsetting sale or purchase of the same security in a different market at as nearly the same time as practicable, for the purpose of taking advantage of a difference in prices in the two markets, or (2) a purchase of a security which is, without restriction other than the payment of money, exchangeable or convertible within 90 calendar days following the date of its purchase into a second security together with an offsetting sale at or about the same time of such second security, for the purpose of taking advantage of a disparity in the prices of the two securities.

(e) *Special commodity account.* In a special commodity account, a creditor may effect and carry for any customer transactions in commodities.

(f) *Special miscellaneous account.* In a special miscellaneous account, a creditor may:

(1) With the approval of any regularly constituted committee of a national securities exchange having jurisdiction over the business conduct of its members, extend and maintain credit to meet the emergency needs of any creditor;

(2) (i) Extend and maintain credit, (a) to or for any partner of a firm which is a member of a national securities exchange to enable such partner to make a contribution of capital to such firm, or to purchase stock in an affiliated corporation of such firm; or (b) to or for any person who is or will become the holder of stock of a corporation which is a member of a national securities exchange to enable such person to purchase stock in such corporation, or to purchase stock in an affiliated corporation of such corporation; provided the lender as well as the borrower is a partner in such member firm or a stockholder in such member corporation, or the lender is a firm or a stockholder in such member corporation, or the lender is a firm or corporation which is a member of a national securities exchange and the borrower is a partner in such firm or a stockholder in such corporation;

(ii) Extend and maintain subordinated credit to another creditor for capital purposes: *Provided*, That,

(a) Either the lender or the borrower is a firm or corporation which is a member of a national securities exchange, the other party to the credit is an affiliated corporation of such member firm or cor-

poration, and, in addition to the fact that an appropriate committee of the exchange is satisfied that the credit that is not in contravention of any rule of the exchange, the credit has the approval of such committee, or

(b) The lender as well as the borrower is a member of such exchange, the credit has the approval of an appropriate committee of the exchange, and the committee, in addition to being satisfied that the credit is not in contravention of any rule of the exchange, is satisfied that the credit is outside the ordinary course of the lender's business, and that, if the borrower's firm or corporation or an affiliated corporation of such firm or corporation does any dealing in securities for its own account, the credit is not for the purpose of increasing the amount of such dealing.

(iii) For the purpose of subdivisions (i) and (ii) of this subparagraph, the term "affiliated corporation" means a corporation all the common stock of which is owned directly or indirectly by the member firm or general partners and employees of the firm, or by the member corporation or holders of voting stock and employees of the corporation and an appropriate committee of the exchange has approved the member firm's or member corporation's affiliation with such affiliated corporation.

(3) Purchase any security from any customer who is a broker or dealer, or sell any security to such customer: *Provided*, That the creditor acting in good faith purchases or sells the security for delivery, against full payment of the purchase price, as promptly as practicable in accordance with the ordinary usage of the trade;

(4) Effect and finance, for any member of a national securities exchange who is registered and acts as odd-lot dealer in securities on the exchange, such member's transactions as an odd-lot dealer in such securities, or effect and finance, for any joint venture in which the creditor participates, any transactions in any securities of an issue with respect to which all participants, or all participants other than the creditor, are registered and act on a national securities exchange as odd-lot dealers;

(5) Effect transactions for and finance any joint venture or group in which the creditor participates and in which all participants are dealers (whether such participants be acting jointly or severally), or any member thereof or participant therein, for the purpose of facilitating the underwriting or distributing of all or part of an issue of securities (i) not through medium of a national securities exchange, or (ii) the distribution of which has been approved by the appropriate committee of a national securities exchange;

(6) Effect for any customer the collection or exchange (other than by sale or purchase) of securities deposited by the customer specifically for such purposes, and (subject to any other applicable provisions of law) receive from or for any customer, and pay out or deliver to or for any customer, any money or securities;

(7) Effect and carry for any customer transactions in foreign exchange; and

(8) Extend and maintain credit to or for any customer without collateral or on any collateral whatever for any purpose other than purchasing or carrying or trading in securities.

(g) *Specialist's account.* In a special account designated as a specialist's account, a creditor may effect and finance, for any member of a national securities exchange who is registered and acts as a specialist in securities on the exchange, such member's transactions as a specialist in such securities, or effect and finance, for any joint venture in which the creditor participates, any transactions in any securities of an issue with respect to which all participants, or all participants other than the creditor, are registered and act on a national securities exchange as specialists. Such specialist's account shall be subject to the same conditions to which it would be subject if it were a general account except that if the specialist's exchange, in addition to the other requirements applicable to specialists, is designated by the Board of Governors of the Federal Reserve System as requiring reports suitable for supplying current information regarding specialists' use of credit pursuant to this paragraph, the requirements of § 220.6 (b) regarding joint ventures shall not apply to such accounts and the maximum loan value of a registered security in such account shall be as determined by the creditor in good faith.

(h) *Special subscriptions account.* In a special subscriptions account a creditor may effect and finance the acquisition of a regulated security for a customer through the exercise of a right to acquire such security which is evidenced by a warrant or certificate issued to stockholders and expiring within 90 days of issuance, and such special subscriptions account shall be subject to the same conditions to which it would be subject if it were a general account, except that:

(1) Each such acquisition shall be treated separately in the account, and prior to initiating the transaction the creditor shall obtain a deposit of cash in the account such that the cash deposited plus the maximum loan value of the securities so acquired equals or exceeds the subscription price, giving effect to a maximum loan value for the securities so acquired of 75 percent of their current market value as determined by any reasonable method;

(2) After October 20, 1967, at the time when credit is extended pursuant to this paragraph, the creditor shall compute the amount by which the credit exceeds the maximum loan value of the collateral as prescribed by § 220.8 (the Supplement to Regulation T) and the customer shall reduce the credit by an amount equal to at least one-fourth of such sum by the end of each of the four succeeding 3-calendar-month periods or until the credit does not exceed the current maximum loan value of the collateral, whichever shall occur first, and, if the creditor fails to obtain the required quarterly reduction or a portion thereof with respect to a particular

acquisition within 5 full business days after such reduction is due, the creditor shall promptly liquidate a portion of the collateral so acquired and apply the proceeds of the sale to reduce the credit, in an amount equal to at least twice the required payment or portion thereof for the first two such liquidations, at least equal to the required payment or portion thereof for the third such liquidation, and at least sufficient so that the remaining credit does not exceed the current maximum loan value of the remaining collateral after the fourth such liquidation: *Provided*, That, no such liquidation need be in an amount greater than is necessary so that the remaining credit does not exceed the maximum loan value of the remaining collateral determined as of the date the credit was extended: *And provided further*, That as to loans made between October 20, 1967, and March 11, 1968, such four succeeding periods shall begin on March 11, 1968; and

(3) The creditor shall not permit any withdrawal of cash or securities from the account so long as the remaining credit exceeds the maximum loan value of the remaining collateral in the account, except that when the remaining credit extended in connection with a given acquisition of securities in the account has become equal to or less than the maximum loan value of such securities as prescribed in § 220.8 (the Supplement to Regulation T) (or in connection with an acquisition after October 20, 1967, the requirements of subparagraph (2) of this section have been fulfilled), such securities shall be transferred to the general account (or, if eligible, to a special convertible security account pursuant to § 220.4(j)) together with any remaining portion of such credit. In order to facilitate the exercise of a right in accordance with the provisions of this paragraph, a creditor may permit the right to be transferred from a general account to the special subscriptions account without regard to any other requirement of this part.

(i) *Special bond account.* In a special bond account a creditor may effect and finance transactions in exempted securities and registered nonequity securities for any customer.

(j) *Special convertible debt security account.* (1) In a special convertible debt security account a creditor may extend credit on any regulated security consisting of a debt security convertible into regulated stock or a debt security carrying a warrant or right to subscribe to or purchase such stock.

(2) A special convertible debt security account shall be subject to the same conditions to which it would be subject if it were a general account except that the maximum loan value of the securities in the account shall be as prescribed from time to time in § 220.8 (the Supplement to Regulation T).

(3) Any security which ceases to be an equity security while held in this account shall continue to be treated as an equity security as long as it is continuously held in this account.

(4) In the event any stock is to be substituted for a security held in this account, or if a security held in this account is to be used to offset a short sale in the general account, such security shall thereupon be transferred to the customer's general account against a deposit of cash or regulated equity securities eligible for an extension of credit in this account (counted at their maximum loan value) equal to at least the maximum loan value of the security for which such substitution is made, without regard to the retention requirement of § 220.3(b)(2).

§ 220.5 Borrowing by members, brokers, and dealers.

(a) *General rule.* It is unlawful for any creditor, directly or indirectly, to borrow in the ordinary course of business as a broker or dealer on any registered security (other than an exempted security) except:

(1) From or through a member bank of the Federal Reserve System; or

(2) From any nonmember bank which shall have filed with the Board an agreement which is still in force and which is in the form prescribed by this Part; or

(3) To the extent to which, under the provisions of this Part, loans are permitted between members of a national securities exchange and/or brokers and/or dealers, or loans are permitted to meet emergency needs.

(b) *Agreements of nonmember banks.* An agreement filed pursuant to section 8(a) of the Act (15 U.S.C. 78h(a)) by a bank not a member of the Federal Reserve System shall be substantially in the form contained in Form F.R. T-2 if the bank has its principal place of business in a territory or insular possession of the United States, or if it has an office or agency in the United States and its principal place of business outside the United States. The agreement filed by any other nonmember bank shall be in substantially the form contained in Form F.R. T-1. Any nonmember bank which has executed any such agreement may terminate the agreement if it obtains the written consent of the Board. Blank forms of such agreements, information regarding their filing or termination, and information regarding the names of nonmember banks for which such agreements are in force, may be obtained from any Federal Reserve Bank.

(c) *Borrowing from other creditors.* A creditor may borrow from another creditor in the ordinary course of business as a broker or dealer on any registered security to the extent and subject to the terms upon which the latter may extend credit to him in accordance with the provisions of this part, and subject to any other applicable provisions of law.

§ 220.6 Certain technical details.

(a) *Accounts of partners.* In case a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j) is the account of a partner of the creditor, the creditor, in calculating the adjusted debit balance of such account and

the maximum loan value of the securities therein, shall disregard the partner's financial relations with the firm as reflected in his capital and ordinary drawing accounts.

(b) *Contribution to joint venture.* In case a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j) is the account of a joint venture in which the creditor participates, the adjusted debit balance of such account shall include, in addition to the items specified in § 22.3(d), any amount by which the creditor's contribution to the joint venture exceeds the contribution which he would have made if he had contributed merely in proportion to his right to share in the profits of the joint venture.

(c) *Guaranteed accounts.* No guarantee of a customer's account shall be given any effect for purposes of this part.

(d) *Transfer of accounts.* (1) In the event of the transfer of a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j) from one creditor to another, such account may be treated for the purposes of this part as if it had been maintained by the transferee from the date of its origin: *Provided*, That, the transferee accepts in good faith a signed statement of the transferor that no cash or securities need be deposited in such account in connection with any transaction that has been effected in such account or, in case he finds that it is not practicable to obtain such a statement from the transferor, accepts in good faith such a signed statement from the customer.

(2) In the event of the transfer of a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j), from one customer to another, or to others, as a bona fide incident to a transaction that is not undertaken for the purpose of avoiding the requirements of this part, each such transferee account may be treated by the creditor for the purposes of this part as if it had been maintained for the transferee from the date of its origin: *Provided*, That, the creditor accepts in good faith and keeps with such transferee account a signed statement of the transferor describing the circumstances giving rise to the transfer.

(e) *Reorganizations.* A creditor may, without regard to the other provisions of this Part, effect for a customer the exchange of any regulated or exempted security in a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j), for the purpose of participating in a reorganization or recapitalization in which the security is involved: *Provided*, That if an unregulated non-exempted security is acquired in exchange, the creditor shall not, for a period of 60 days following such acquisition, permit the withdrawal of such security or the proceeds of its sale from such account except to the extent that such security or proceeds could be withdrawn if the security were a regulated security.

(f) *Time of receipt of funds or securities.* For the purposes of this part, a creditor may, at his option (1) treat the receipt in good faith of any check or draft drawn on a bank which in the ordinary course of business is payable on presentation, or any order on a savings bank with passbook attached which is so payable, as receipt of payment of the amount of such check, draft or order; (2) treat the shipment of securities in good faith with sight draft attached as receipt of payment of the amount of such sight draft; and (3) in the case of the receipt in good faith of written or telegraphic notice in connection with a special omnibus account of a customer not located in the same city that a specified security or a check or draft has been dispatched to the creditor, treat the receipt of such notice as receipt of such security, check, or draft: *Provided, however*, That if the creditor receives notice that such check, draft, order, or sight draft described in subparagraphs (1), (2), or (3) of this paragraph is not paid on the day of presentation, or if such security, check or draft described in subparagraph (3) of this paragraph is not received by the creditor within a reasonable time, the creditor shall promptly take such action as he would have been required to take by the appropriate provisions of this part if the provisions of this paragraph had not been utilized.

(g) *Interest, service charges, etc.* (1) Interest on credit maintained in a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j), communication charges with respect to transactions in such account, shipping charges, premiums on securities borrowed in connection with short sales or to effect delivery, dividends or other distributions due on borrowed securities, and any service charges (other than commissions) which the creditor may impose, may be debited to such account in accordance with the usual practice and without regard to the other provisions of this part, but such items so debited shall be taken into consideration in calculating the net credit or net debit balance of such account.

(2) A creditor may permit interest, dividends or other distributions received by the creditor with respect to securities in a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j), to be withdrawn from such account only on condition that the adjusted debit balance of such account does not exceed the maximum loan value of the securities in such account after such withdrawal, or on condition that (i) such withdrawal is made within 35 days after the day on which, in accordance with the creditor's usual practice, such interest, dividends or other distributions are entered in such account, (ii) such entry in the account has not served in the meantime to permit in the account any transaction which could not otherwise have been effected in accordance with this part, and (iii) any cash withdrawn does not represent any

arrears on the security with respect to which it was distributed, and the current market value of any securities withdrawn does not exceed 10 percent of the current market value of the security with respect to which they were distributed. Failure by a creditor to obtain in a general account, special bond account subject to § 220.4(i), or special convertible security account subject to § 220.4(j), any cash or securities that are distributed with respect to any security in such account shall, except to the extent that withdrawal would be permitted under the preceding sentence, be deemed to be a transaction in such account which occurs on the day on which the distribution is payable and which requires the creditor to obtain in accordance with § 220.3(b) a deposit of cash or securities having a maximum loan value at least as great as that of the distribution.

(h) *Borrowing and lending securities.* Without regard to the other provisions of this part, a creditor (1) may make a bona fide deposit of cash in order to borrow securities (whether regulated or unregulated) for the purpose of making delivery of such securities in the case of short sales, failure to receive securities he is required to deliver, or other similar cases, and (2) may lend securities for such purpose against such a deposit.

(i) *Credit for clearance of securities.* The extension or maintenance of any credit which is maintained for only a fraction of a day (that is, for only part of the time between the beginning of business and midnight on the same day) shall be disregarded for the purposes of this part, if it is incidental to the clearance of transactions in securities directly between members of a national securities exchange or through an agency organized or employed by such members for the purpose of effecting such clearance.

(j) *Foreign currency.* If foreign currency is capable of being converted without restriction into U.S. currency, a creditor acting in good faith may treat any such foreign currency in an account as a credit to the account in an amount determined in accordance with customary practice.

(k) *Innocent mistakes.* If any failure to comply with this part results from a mechanical mistake made in good faith in executing a transaction, recording, determining, or calculating any loan, balance, market price or loan value, or other similar mechanical mistake, the creditor shall not be deemed guilty of a violation of this part if promptly after the discovery of such mistake he takes whatever action may be practicable in the circumstances to remedy such mistake.

§ 220.7 Miscellaneous provisions.

(a) *Arranging for loans by others.* A creditor may arrange for the extension or maintenance of credit to or for any customer of such creditor by any person upon the same terms and conditions as those upon which the creditor, under the provisions of this part, may himself extend or maintain such credit to such customer, but only upon such terms and

conditions, except that this limitation shall not apply with respect to the arranging by a creditor for a bank subject to Part 221 of this chapter (Regulation U) to extend or maintain credit on regulated securities or exempted securities.

(b) *Maintenance of credit.* Except as otherwise specifically forbidden by this part, any credit initially extended without violation of this part may be maintained regardless of (1) reductions in the customer's equity resulting from changes in market prices, (2) the fact that any security in an account ceases to be regulated or exempted, and (3) any change in the maximum loan values or margin requirements prescribed by the Board under this part. In maintaining any such credit, the creditor may accept or retain for his own protection additional collateral of any description, including unregulated securities.

(c) *Declaration as to purpose of loan.* Every extension of credit on a regulated security (other than an exempted security) shall be deemed to be for the purpose of purchasing or carrying or trading in securities, unless the creditor has accepted in good faith a written statement to the contrary in conformity with the requirements of Federal Reserve Form T-4 executed by the customer and executed and accepted in good faith by the creditor prior to such extension. The creditor shall retain such statement in his records for at least 3 years after such credit is extinguished. To accept the customer's statement in good faith, the creditor must (1) be alert to the circumstance surrounding the extension of credit and (2) if he has any information which would cause a prudent man not to accept the statement without inquiry, have investigated and be satisfied that the customer's statement is truthful. A creditor may rely upon such a written statement if accepted in accordance with this paragraph.

(d) *Reports.* Every creditor shall make such reports as the Board may require to enable the Board to perform the functions conferred upon it by the Act.

(e) *Additional requirements by exchanges and creditors.* Nothing in this part shall (1) prevent any exchange from adopting and enforcing any rule or regulation further restricting the time or manner in which its members must obtain initial or additional margin in customers' accounts because of transactions effected in such accounts, or requiring such members to secure or maintain higher margins, or further restricting the amount of credit which may be extended or maintained by them, or (2) modify or restrict the right of any creditor to require additional security for the maintenance of any credit, to refuse to extend credit, or to sell any securities or property held as collateral for any loan or credit extended by him.

§ 220.8 Supplement.

(a) *Maximum loan value for general accounts.* The maximum loan value of securities in a general account subject to § 220.3 shall be:

(1) of a registered non-equity security held in the account on March 11, 1968, and continuously thereafter and of a regulated equity security (except as provided in § 220.3(c) and § 220.8 (b) and (c)), 20 percent of the current market value of such securities.

(2) of an exempted security held in the account on March 11, 1968, and continuously thereafter the maximum loan value of the security, as determined by the creditor in good faith.

(b) *Maximum loan value for a special bond account.* The maximum loan value of an exempted security and of a registered nonequity security pursuant to § 220.4(i) shall be the maximum loan value of the security as determined by the creditor in good faith.

(c) *Maximum loan value for special convertible debt security account.* The maximum loan value of a regulated equity security eligible for a special convertible security account pursuant to § 220.4(j) shall be 40 percent of the current market value of the security.

(d) *Margin required for short sales.* The amount to be included in the adjusted debit balance of a general account, pursuant to § 220.3(d)(3), as margin required for short sales of securities (other than exempted securities) shall be 80 percent of the current market value of each security.

(e) *Retention requirement.* In the case of an account which would have an excess of the adjusted debit balance of the account over the maximum loan value of the securities in the account following a withdrawal of cash or securities from the account, pursuant to § 220.3(b)(2):

(1) The "retention requirement" of an exempted security held in the general account on March 11, 1968, and continuously thereafter shall be equal to its maximum loan value as determined by the creditor in good faith, and the "retention requirement" of a registered non-equity security held in such account on March 11, 1968, and continuously thereafter and of a regulated security shall be 70 percent of the current market value of the security.

(2) In the case of a special bond account subject to § 220.4(i), the retention requirement of an exempted security and of a registered nonequity security shall be equal to the maximum loan value of the security.

(3) In the case of a special convertible security account subject to § 220.4(j) which would have an excess of the adjusted debit balance of the account over the maximum loan value of the securities in the account following a withdrawal of cash or securities from the account, the retention requirement of a security having loan value in the account shall be 70 percent of the current market value of the security.

(4) For the purpose of effecting a transfer from a general account to a special convertible security account subject to § 220.4(j), the retention requirement of a security described in § 220.4(j), shall be 70 percent of its current market value.

(f) *Security having no loan value in general account.* No securities other than an exempted security or registered non-equity security held in the account on March 11, 1968, and continuously thereafter, and a regulated security shall have any loan value in a general account except that a regulated security eligible for the special convertible security account pursuant to § 220.4(j) shall have loan value only if held in the account on March 11, 1968, and continuously thereafter.

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