FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 7690
August 18, 1975]

PROPOSED AMENDMENT TO REGULATION T

Margin Requirements for Writing Options to Sell or Buy Stock

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

Following is the text of a statement issued August 12 by the Board of Governors of the Federal Reserve System:

The Board of Governors of the Federal Reserve System today issued for comment a revised proposal to amend its Regulation T, designed to prevent the excessive use of credit in connection with the issuance, endorsement or guarantee of puts and calls, which are options to sell or buy stock.

Comment will be received by the Board through September 30.

The principal effect of the proposed amendment to Regulation T—extension of securities credit by brokers and dealers—would be to set the level of margin required for uncovered options at 30 per cent of the market value of the underlying security with additional adjustment for unrealized losses and gains.

No margin would be required where the option is covered, that is, where the security itself, or its equivalent, is held in the option writer's account.

The proposed amendment would apply to the extension of credit by brokers and dealers when they endorse or guarantee options written by their customers. Under a previous Board ruling no credit may be extended for the purchase of an option.

Printed below is the text of the Board's proposal. Comments thereon should be submitted by September 30, and may be sent to our Bank Regulations Department.

Paul A. Volcker,
President.

[Reg. T]

CREDIT BY BROKERS AND DEALERS

Uniform Margin Requirements for Writing Options

By notice of proposed rulemaking published in the *Federal Register* on May 23, 1973 (38 F.R. 13571), the Board of Governors, pursuant to authority contained in the Securities Exchange Act of 1934 (15 U.S.C. 78g), invited comment on a proposal to require a uniform margin in connection with the issuance, endorsement or guarantee of any put, call or combination thereof, based initially upon the current minimum requirements of the major stock exchanges.

Following consideration of all the comments received, and taking into consideration changes made in the rules of the exchanges since the proposal was published, the Board has revised the proposal to require a uniform margin of 30 per cent of the current market value of the underlying security, subject to certain other adjustments as specified in the regulation. The revised proposal is as follows:

In section 220.3, paragraph (d) would be amended and a new paragraph (i) would be added as set forth below:

SECTION 220.3—GENERAL ACCOUNT

* * *

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

* * *

(5) The amount of margin as provided for in paragraph (i) of this section and § 220.8 (the Supplement to Regulation T) for each transaction involving the issuance, endorsement or guarantee of any put, call or combination thereof.

(OVER)

* * *

(i) **Options.** (1) The amount to be included in the adjusted debit balance of a general account as the margin required for each transaction involving the issuance, endorsement or guarantee of any put or call shall be such amount as the Board shall prescribe from time to time in § 220.8 (the Supplement to Regulation T) as the margin required for the writing of options, increased by any unrealized loss on each such commitment, or reduced by any excess of the exercise price over the current market value of the underlying security in the case of a call or any excess of the current market value of the underlying security over the exercise price in the case of a put. Such sum, however, shall not exceed the current market value of the underlying security in the case of a call, or the exercise price in case of a put, nor be less than 10 per cent of the current market value of the underlying security in the case of either a call or a put. Such sum need not be included in the adjusted debit balance when there is held in the general account any of the following:

(i) The underlying security in the case of a call or a short position in the underlying security in the case of a put;

(ii) Securities immediately convertible into or exchangeable for the underlying security without restriction or the payment of money in the case of a call;

(iii) An agreement under which a bank, which is holding the underlying securities or the required cash, is obligated to deliver or accept the underlying securities against payment of the exercise price upon exercise of the option; or

(iv) A long position in a call on the same number of shares of the same underlying security which does not expire before the expiration date of the call issued, endorsed or guaranteed, provided that there is also added to the adjusted debit balance the amount, if any, by which the exercise price of such long position exceeds the exercise price of the call issued, endorsed or guaranteed.

(2) When a security held in the account serves in lieu of the margin required for a call, such security shall be valued at no greater than the exercise price of the call.

(3) When a short position held in the account serves in lieu of the margin required for a put, the amount prescribed by paragraph (d)(3) of this section as the amount to be added to the adjusted debit balance in respect of short sales shall be increased by any unrealized loss on the position.

In section 220.8 (the Supplement to Regulation T) a new paragraph (j) would be added as set forth below:

SECTION 220.8—SUPPLEMENT

* * *

(j) **Margin required for the writing of options.** The amount to be included in the adjusted debit balance of a general account, pursuant to paragraphs (d)(5) and (i) of § 220.3, as margin required for the issuance, endorsement or guarantee of any put or call, adjusted for any applicable increase or reduction, shall be,

(1) of a put, 30 per cent of the exercise price,

(2) of a call, 30 per cent of the current market value of the underlying security.

Interested persons are invited to submit relevant data, views, or arguments concerning this proposal. Any such material should be submitted in writing to the Secretary, Board of Governors of the Federal Reserve System, Washington, D. C. 20551, to be received not later than September 30, 1975. Such material will be made available for inspection and copying upon request, except as provided in § 261.6(a) of the Board's Rules Regarding Availability of Information.

By order of the Board of Governors, August 11, 1975.