

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 9294]
May 19, 1982]

MARGIN REGULATIONS

Changes in Criteria for Inclusion on List of OTC Margin Stocks

To All Banks, Brokers and Dealers, and Persons Extending
Securities Credit in the Second Federal Reserve District:

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

The Federal Reserve Board has adopted amendments to its margin regulations that change the criteria for inclusion on the Board's list of stocks traded over the counter (OTC list).

Inclusion of a stock on this list makes it possible for brokers and dealers to lend on the stock in conformance to the Board's margin requirements. About 1,500 stocks are on the Board's OTC list.

Further, the Board decided that in the future changes in the OTC list, which is updated three times yearly, will become effective two weeks after publication rather than immediately.

The changes adopted by the Board, after consideration of comment received on proposals published last November, are:

1. Inclusion on this list of eligible foreign securities.
2. Setting of mandatory price and capital criteria for determining OTC list eligibility (formerly, stocks, to be eligible, could satisfy any two out of three criteria: price, capital or market value).
3. Reduction of requirements for *initial* listing as follows:
 - Capital requirement of \$4 million (rather than \$5 million), and
 - Requirement for the number of shares held publicly lowered to 400,000 (rather than 500,000).
4. Reduction of requirements for *continued* listing as follows:
 - Capital, \$1 million (rather than \$2.5 million).
 - Listed price, \$2 (rather than \$5).

Stocks that no longer meet eligibility requirements under the new criteria for listing on the Board's OTC list will be retained on the list for two years. The Board believes the revised criteria reflect changes, since the last major revision of the criteria in 1976, in stock market conditions and exchange practices.

Printed on the following pages is the summary of the Board's amendments, effective June 12, 1982. The full text will be published in the *Federal Register*, and will also be furnished upon request directed to our Circulars Division (Tel. No. 212-791-5216).

Questions on this matter may be directed to our Regulations Division (Tel. No. 212-791-5914).

ANTHONY M. SOLOMON,
President.

FEDERAL RESERVE SYSTEM

Regulations G, T and U

[12 CFR 207, 220 and 221]

[Docket No. R-0372]

SECURITIES CREDIT TRANSACTIONS

Revision of Criteria for Initial and Continued Inclusion
on the List of OTC Margin Stocks

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final Rule.

SUMMARY: On November 24, 1981, the Board published for comment (46 Fed. Reg. 57532) a proposal to amend its criteria for initial and continued inclusion on the List of OTC Margin Stocks ("OTC List"). Brokers and dealers may not extend credit on stocks which are traded over-the-counter unless such stocks appear on the OTC List. Loans by banks and other lenders that are used to purchase stocks appearing on the OTC List are subject to the Board's margin requirements if the loans are secured by margin stock.

In its announcement, the Board proposed to revise OTC List criteria in three important respects. First, equity securities of foreign issuers and American Depository Receipts would, for the first time, be eligible for OTC List inclusion. Second, certain alternative criteria with respect to price and capital were to be made mandatory. Third, a proposal was made to relax capital and price criteria to more closely resemble the listing requirements of major stock exchanges.

In its action today, the Board adopts revisions to OTC List criteria in substantially the same form as proposed. Specifically, the OTC List criteria are amended to (1) permit the inclusion of securities of foreign issuers registered with the Securities and Exchange Commission, (2) eliminate the alternative market value criterion and make the price and capital criteria mandatory, (3) reduce the initial listing capital and publicly-held share criteria to \$4 million and 400,000 shares, respectively, and (4) reduce the continued listing price and capital criteria to \$2 and \$1 million, respectively.

In response to public commentary, the price requirement for continued listing adopted by the Board today is higher than that originally proposed for comment but lower than that in the existing rule. The Board wishes to make clear that its action today with respect to the inclusion of foreign issuers on the OTC List is limited to those issuers who have actually registered with the Securities and Exchange Commission or file reports comparable to those filed by domestic companies.

In order to give brokers and service bureaus time to adjust their programs to reflect changes in the OTC List, the Board will hereafter publish the OTC List two weeks in advance of its effective date. This change was suggested by many commenters.

The Board wishes to make clear that no existing OTC margin stock which ceases to meet new OTC List criteria will be immediately removed from the OTC List as a result of these amendments; the Board intends to "grandfather" such stocks for two years. Interested persons should also be aware that special consideration for inclusion on the List will be given to companies which voluntarily file an application to delist their securities from a national exchange and are trading in NASDAQ. Such a procedure will prevent any interruption in the marginability of certain securities.

EFFECTIVE DATE: June 12, 1982.

FOR FURTHER INFORMATION CONTACT: Jamie Lenoci, Financial Analyst, or Robert Lord, Attorney, Division of Banking Supervision and Regulation (202) 452-2781.

SUPPLEMENTARY INFORMATION: In July 1969, pursuant to the Over the Counter Market Act of 1968, (Pub. L. 90-437), the Board adopted criteria which, if met by issuers of over-the-counter stocks, would result in the stocks being placed on the OTC List and hence afforded the same treatment as exchange listed stocks for purposes of the Board's margin rules. This meant that once on the OTC List, over-the-counter stocks were eligible for margin trading. In addition to criteria for initial eligibility for the OTC List, criteria for continued eligibility for inclusion on the OTC List were also established by the Board in 1972.

Changes in the OTC List criteria made today are the result of a review of recent developments in the securities markets, particularly the OTC market, staff experience with the administration of the OTC List and the public commentary. Each change is discussed below.

Foreign Issuers Now Eligible for OTC List Inclusion

Issuers eligible for inclusion on the OTC List will no longer have to be organized under the laws of the United States or a State. Foreign issuers were precluded from OTC List eligibility in the past because of the relative lack of access to such issuers' financial information. The strengthened disclosure rules of the Securities and Exchange Commission now make it possible to obtain comprehensive and up to date financial information on many foreign issuers. Because of these improvements, it is no longer necessary to restrict OTC List candidates to domestic issuers. Foreign as well as domestic issuers must, however, be registered or file comparable reports with the Securities and Exchange Commission in order to be eligible for inclusion on the OTC List.

Eliminating Alternate Criteria and Making Price and Capital Criteria Mandatory

Another change in OTC List criteria involves the alternative requirements with respect to the size and character of the issue and issuer. Prior to these amendments, a stock could fail one of the three criteria of a \$5.00 minimum price, \$5 million capital, or \$5 million in market value and still be placed on the OTC List. The criterion requiring an aggregate market

value of \$5 million is of limited value in determining OTC List eligibility since it only affects stocks worth between \$5 and \$10 per share. During the past two years, for example, only seven per cent of the stocks added to the OTC List failed the aggregate market value test. Accordingly, the retention of this test is no longer justified.

The remaining alternate criteria for both initial and continued inclusion on the OTC List -- relating to price per share and minimum capital -- are now made mandatory. Doing so will lessen the effect of systemic fluctuations which have indirectly been affecting the size and composition of the OTC List.

The Board originally proposed to lower the price and capital criteria for continued listing from \$3 and \$2.5 million to \$1 and \$1 million, respectively. Some public comment, however, reflected the view that the proposed criteria may encourage the use of speculative credit. The Board has decided, therefore, to adopt a higher continued listing price criterion than that proposed. The new criterion will still be lower than the criterion existing before these amendments. The capital criterion for initial and continued listing has been reduced to \$4 million and \$1 million, respectively. The initial listing price per share criterion will remain at \$5. The continued listing price per share criterion has been reduced to \$2. The initial listing publicly held share criterion has been reduced to 400,000 shares. These changes will make the Board's OTC List criteria more comparable to the listing criteria of the American Stock Exchange.

(NOTE: The remainder of this notice may be obtained from the Federal Reserve Board or the Federal Reserve Banks.)

FEDERAL RESERVE SYSTEM

Regulations G, T and U

[12 CFR 207, 220 and 221]

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List of Subject Headings in 12 CFR Part 207

Banks, banking; Credit; Federal Reserve System; Margin; Margin Requirements; Reporting requirements; Securities

List of Subject Headings in 12 CFR Part 220

Banks; banking; Brokers; Credit; Federal Reserve System; Margin; Margin Requirements; Investments; Reporting requirements; Securities

List of Subject Heading in 12 CFR Part 221

Banks, banking; Credit; Federal Reserve System; Margin; Margin Requirements; Reporting requirements; Securities

Accordingly, pursuant to §§ 7 and 23 of the Securities Exchange Act of 1934, as amended (15 U.S.C. §§ 78g, 78w), the Board amends Regulations G, T and U (12 CFR Parts 207, 220 and 221, respectively) as follows:

PART 207 -- SECURITIES CREDIT BY PERSONS OTHER THAN BANKS, BROKERS, OR DEALERS

A. Section 207.5 -- Supplement

* * * * *

(d) Requirements for inclusion on list of OTC margin stocks

(1) The stock is registered under section 12 of the Act (15 U.S.C. 781), is issued by an insurance company subject to section 12(g)(2)(G) (15 U.S.C. § 781(g)(2)(G)), is issued by a closed-end investment management company subject to registration pursuant to section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), is an American Depository Receipt of a foreign issuer

whose securities are registered under section 12 of the Act, or is a stock of an issuer required to file reports under section 15(d) of the Act (15 U.S.C. 78o(d)),

* * *

(4) the issuer or a predecessor in interest has been in existence for at least three years,

* * *

(7) There are 400,000 or more shares of such stock outstanding in addition to shares held beneficially by officers, directors, or beneficial owners of more than 10 per cent of the stock,

(8) The minimum average bid price of such stock, as determined by the Board, is at least \$5 per share, and

(9) The issuer has at least \$4 million of capital, surplus, and undivided profits.

(e) Requirements for continued inclusion on list of OTC margin stocks

(1) The stock continues to be registered under section 12 of the Act (15 U.S.C. 781), or if issued by an insurance company such issuer continues to be subject to section 12(g)(2)(G)(15 U.S.C. 781(g)(2)(G)), or if issued by a closed-end investment management company such issuer continues to be subject to registration pursuant to section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), is an American Depository Receipt of a foreign issuer whose securities are registered under section 12 of the Act, or is a stock of an issuer required to file reports under section 15(d) of the Act (15 U.S.C. 78o(d)),

* * *

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

(5) There are 300,000 or more shares of such stock outstanding in addition to shares held beneficially by officers, directors, or beneficial owners of more than 10 per cent of the stock,

(6) The minimum average bid price of such stocks, as determined by the Board, is at least \$2 per share, and

(7) The issuer has at least \$1 million of capital, surplus, and undivided profits.

PART 220 -- CREDIT BY BROKERS AND DEALERS

A. Section 220.8 -- Supplement

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(h) Requirements for inclusion on list of OTC margin stocks

(1) The stock is registered under section 12 of the Act (15 U.S.C. 781), is issued by an insurance company subject to section 12(g)(2)(G)(15 U.S.C. § 781(g)(2)(G)), is issued by a closed-end investment management company subject to registration pursuant to section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), is an American Depository Receipt of a foreign issuer whose securities are registered under section 12 of the Act, or is a stock of an issuer required to file reports under section 15(d) of the Act (15 U.S.C. 78o(d)),

* * *

(4) the issuer or a predecessor in interest has been in existence for at least three years,

* * *

(7) There are 400,000 or more shares of such stock outstanding in addition to shares held beneficially by officers, directors, or beneficial owners of more than 10 per cent of the stock,

(8) The minimum average bid price of such stock, as determined by the Board, is at least \$5 per share, and

(9) The issuer has at least \$4 million of capital, surplus, and undivided profits.

(i) Requirements for continued inclusion on list of OTC margin stocks

(1) The stock continues to be registered under section 12 of the Act (15 U.S.C. 781), or if issued by an insurance company such issuer continues to be subject to section 12(g)(2)(G)(15 U.S.C. 781(g)(2)(G)), or if issued by a closed-end investment management company such issuer continues to be subject to registration pursuant to section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), is an American Depository Receipt of a foreign issuer whose securities are registered under section 12 of the Act, or is a stock of an issuer required to file reports under section 15(d) of the Act (15 U.S.C. 78o(d)),

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

(5) There are 300,000 or more shares of such stock outstanding in addition to shares held beneficially by officers, directors, or beneficial owners of more than 10 per cent of the stock,

(6) The minimum average bid price of such stocks, as determined by the Board, is at least \$2 per share, and

(7) The issuer has at least \$1 million of capital, surplus, and undivided profits.

PART 221 -- CREDIT BY BANKS FOR THE PURPOSE OF PURCHASING OR CARRYING MARGIN STOCKS

III. A. Section 221.4 -- SUPPLEMENT

* * * * *

(d) Requirements for inclusion on list of OTC margin stocks

(1) The stock is registered under section 12 of the Act (15 U.S.C. 781), is issued by an insurance company subject to section 12(g)(2)(G)(15 U.S.C. § 781(g)(2)(G)), is issued by a closed-end investment management company subject to registration pursuant to section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), is an American Depository Receipt of a foreign issuer whose securities are registered under section 12 of the Act, or is a stock of an issuer required to file reports under section 15(d) of the Act (15 U.S.C. 780(d),

* * * * *

(4) the issuer or a predecessor in interest has been in existence for at least three years,

* * * * *

(7) There are 400,000 or more shares of such stock outstanding in addition to shares held beneficially by officers, directors or beneficial owners of more than 10 per cent of the stock,

(8) The minimum average bid price of such stock, as determined by the Board, is at least \$5 per share, and

(9) The issuer has at least \$4 million of capital, surplus, and undivided profits.

(e) Requirements for continued inclusion on list of OTC margin stocks

(1) The stock continues to be registered under section 12 of the Act (15 U.S.C. 781), or if issued by an insurance company such issuer continues to be subject to section 12(g)(2)(G)(15 U.S.C. 781(g)(2)(G)), or if issued by a closed-end investment management company such issuer continues to be subject to registration pursuant to section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), is an American Depository Receipt of a foreign issuer whose securities are registered under section 12 of the Act, or is a stock of an issuer required to file reports under section 15(d) of the Act (15 U.S.C. 780(d)),

* * * * *

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

(5) There are 300,000 or more shares of such stock outstanding in addition to shares held beneficially by officers, directors, or beneficial owners of more than 10 per cent of the stock,

(6) The minimum average bid price of such stock, as determined by the Board, is at least \$2 per share, and

(7) The issuer has at least \$1 million of capital, surplus, and undivided profits.

FINAL REGULATORY FLEXIBILITY ANALYSIS:

The initial regulatory flexibility analysis indicated that because the proposals to amend OTC List criteria involved a mixture of relaxing and tightening changes, it was not easy to judge the overall impact on small domestic entities -- primarily those small-sized corporations whose stocks are traded in the over-the-counter market.

No comments were received which would lead the Board to conclude that the adoption of these amendments would have a significant economic impact on a substantial number of small entities.

By order of the Board of Governors of the Federal Reserve System,
May 12, 1982.

(Signed) William W. Wiles
William W. Wiles
Secretary of the Board

[SEAL]