

**FEDERAL RESERVE BANK  
OF NEW YORK**

[ Circular No. 9729  
September 19, 1984 ]

**MARGIN REGULATIONS**

**Amendments to Regulations G, T, and U  
Permitting Brokers and Dealers to Make Margin Loans  
On Certain Over-the-Counter Securities**

*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 announced adoption of amendments to its Regulations G, T and U (margin requirements) to automatically permit brokers and dealers to lend on over-the-counter securities designated for trading in the National Market System (NMS) portion of NASDAQ<sup>1</sup> in conformance with the Board's margin requirements. The amendments are effective November 13, 1984.

The Board acted after consideration of comment received on proposals published March 12, 1984. The proposed amendments were adopted substantially as proposed.

The National Market System list of securities was developed in response to a legislative mandate to the Securities and Exchange Commission (SEC) to facilitate and regulate development of a market system linking securities markets through uniform reporting systems. Unlike other securities traded in the over-the-counter (OTC) market, "last sale" reporting is required of National Market System securities. Stocks are included in the National Market System under two sets of criteria developed by the NASD with the approval of the SEC. Currently, there are 1,050 stocks traded in the National Market System.

The amendments provide that OTC securities will automatically become "margin securities" upon the effective date of their designation by the NASD as NMS securities. In order to keep the public fully informed as to which OTC stocks are subject to margin, the Board will publish quarterly a List of OTC Margin Stocks. This will include stocks that have been designated NMS securities in the interim between Board publication of its OTC list of margin stocks.

Information concerning interim designations of NMS securities, or other OTC securities subject to margin, may be obtained from the Public Reference Branch of the Securities and Exchange Commission (Tel. No. 202-272-7450), from the Federal Reserve Board (Tel. No. 202-452-2781), or from the Federal Reserve Banks.

Language has been added to Regulation U to protect banks and to Regulation G to protect lenders under that regulation who extend credit on securities in the interim between Board publication of OTC stock lists without notification that an OTC stock has been designated an NMS security.

<sup>1</sup> National Association of Securities Dealers Automated Quotations System.

Enclosed is a copy of the text of the amendments, effective November 13, 1984, which have been reprinted from the *Federal Register*. A copy of the Board's List of OTC Margin Stocks containing those stocks that have been designated NMS securities will be sent to you as soon as it is available.

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

ANTHONY M. SOLOMON,  
*President.*

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

SECURITIES CREDIT TRANSACTIONS

AMENDMENTS TO REGULATIONS G, T, AND U

(effective November 13, 1984)

**FEDERAL RESERVE SYSTEM**

**12 CFR Parts 207, 220, and 221**

**Regulations G, T and U; Securities Credit Transactions; Amendment to definitions of "margin security" and "margin stock" and related technical amendments**

[Docket No. R-0512]

**AGENCY:** Board of Governors of the Federal Reserve System.

**ACTION:** Final rule.

**SUMMARY:** The Board is amending the definition of "margin security" in Regulation T and the definitions of "margin stock" in Regulations G and U to give automatic marginability to any over-the-counter security identified as a National Market System (NMS) security in accordance with a designation plan of the National Association of Securities Dealers (NASD) that has been approved by the Securities and Exchange Commission (SEC). The Board will publish the List of OTC Margin Stocks on a new quarterly schedule. The Board's List will include NMS and non-NMS securities that otherwise meet the criteria for marginability established by the Board. Regulations G and U are also being amended to provide protection for lenders who may not have notice of a stock's designation between the Board's quarterly publication dates.

**EFFECTIVE DATE:** November 13, 1984.

**FOR FURTHER INFORMATION CONTACT:** Robert S. Plotkin, Assistant Director, Laura Homer, Securities Credit Officer, or Jamie Lenoci, Financial Analyst, Division of Banking Supervision and Regulation, (202) 452-2781.

**SUPPLEMENTARY INFORMATION:**

**I. History of Amendment**

In response to a petition of the NASD, the Board published a proposed amendment to the margin regulations for comment that would give automatic marginability to any over-the-counter security designated as a National Market System (NMS) security (49 FR 9741, March 15, 1984). The Board is adopting the amendment in substantially the same form as proposed. However, due to comments received, the amendment has been technically revised to address some of the concerns of the respondents. In particular, language has been added to Regulations G and U to provide protection against inadvertent violations by lenders covered by those regulations who may not have actual notice that a particular stock has been designated as an NMS security. A similar provision is not being added to Regulation T because a broker is prohibited by statute from extending credit on securities that are not marginable; therefore such a provision is unnecessary.

**Determination of Status of OTC Stock's Marginability**

An OTC stock can become marginable (1) by meeting the criteria

specified by the Board in its margin regulations (Regulations G, T and U) and actual inclusion on the Board's List of OTC Margin Stocks, or (2) by being designated as an NMS security in accordance with the designation plan of the NASD that has been approved by the SEC. Under SEC Rule 11Aa2-1 (17 CFR 240.11Aa2-1), the qualification date for determining a "Tier 1" NMS security (which is a mandatory designation) is the last business day of the calendar quarter. To become a "Tier 2" NMS security (which is a voluntary designation) the issuer must meet "Tier 2" qualifying criteria and must apply for the NMS designation. Under the NASD's present procedures, it is contemplated that, in general, "Tier 2" NMS stocks will be added not more than once every other week. Notice will be given to the industry and regulators by the NASD at least one week prior to the effective date of the designation which, in the case of an initial public offering of a security, may be on a "when, as, and if issued" basis.

In order to keep the public fully aware of which OTC stocks are marginable, the Board will publish quarterly a complete List of OTC Margin Stocks. This hard-copy publication will be on file at the Federal Register and can be obtained from the Board or any Federal Reserve Bank. In addition, the Board will publish a Supplement of additions to and deletions from the List of OTC Margin Stocks on a quarterly basis in the Federal Register. This Supplement will include current NMS securities as

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For this Regulation to be complete, retain:

- 1) Pamphlet dated December 1983, entitled "Securities Credit Transactions."
- 2) Amendment and corrections to Regulation T, effective April 13, 1984 (included in slip sheet, dated July 1984).
- 3) This slip sheet.

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well as those securities deemed marginable under the Board's margin criteria. The publication of these Supplements will be timed to coincide with the NASD's quarterly inclusion of Tier 1 NMS securities. Since the next designation of the Tier 1 NMS securities is expected to be effective on November 13, 1984, the Board's Supplement to the List, ordinarily effective in October, will be delayed to coincide with this November date. Future Supplements of additions to and deletions from the List will be published quarterly in the Federal Register at the end of January, April, July and October with the usual two-week delayed effective date. There will be no SEC publication of NMS securities in the Federal Register as contemplated in the Board's original proposal.

Additional OTC securities may be designated by the NASD as NMS securities in the interim between Board publications. These securities will be automatically marginable at broker-dealers upon the effective date of their designation. A list of these securities and the effective date of their designation will be available at the Public Reference Branch of the SEC and copies will be hand delivered to the Board and delivered by overnight express to each of the Reserve Banks. Banks, broker-dealers, Regulation G lenders and other persons can verify whether an OTC stock is an NMS security by calling the SEC at its Public Reference Branch, 450 5th Street, NW., Washington, D.C. 20549 ((202) 272-7450). The margin status of any OTC stock can be obtained by calling the Securities Regulation Section in the Board's Division of Banking Supervision and Regulation ((202) 452-2781) or by calling any Federal Reserve Bank.

#### Final Regulatory Flexibility Analysis

The Board is amending its regulations to give automatic marginability to securities that are designated as qualified for trading in the National Market System. The initial regulatory flexibility analysis indicated that the amendment was not expected to have any adverse impact on a substantial number of small entities.

A comment on the proposed change raised the question of whether the Board

discriminated against small business by not adopting the original NASD proposal, which asked for automatic marginability to securities on the entire National List. The decision to permit National Market System securities to be marginable was based on staff analysis indicating that the liquidity and other characteristics of NMS securities compare favorably with those of exchange-traded securities. A major difference between NMS and other National List securities is that the latter do not have "last sale" reporting, deemed necessary by stock exchanges to assure the availability of reliable price information. In the absence of such information and in light of other evidence suggesting differences in liquidity among National List securities, the Board decided to give automatic marginability at the present time only to National List securities traded in the NMS.

There is no evidence indicating that the regulatory change will have a significant impact on a substantial number of small businesses. If stocks of small entities are traded in the National Market System, they will be marginable at a brokerage firm after the regulatory change becomes effective. Small entities and other companies comprising the approximately 800 National List firms that are not on the NMS and that are not on the Board's List of OTC Margin Stocks will not be automatically marginable but, of course, may become marginable subject to satisfying Board OTC criteria. From the individual corporation's perspective, the economic effect of marginability is mixed. When securities become eligible as collateral in a margin account at a brokerage firm, they also become subject to regulatory limitations on the amount of credit that may be extended against their value by banks and other lenders; such limitations do not apply to nonmarginable stocks at banks and other lenders.

#### List of Subjects

##### 12 CFR Part 207

Banks, Banking, Credit, Margin, Margin requirements, Reporting and recordkeeping requirements, Securities.

##### 12 CFR Part 220

Banks, Banking, Brokers, Credit, Margin, Margin requirements, Investments, Reporting and recordkeeping requirements, Securities.

##### 12 CFR Part 221

Banks, Banking, Credit, Margin, Margin requirements, Reporting and recordkeeping requirements, Securities.

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

Section 207.2—"Definitions", is amended by adding a new paragraph (i)(3), and renumbering (i)(3), (4) and (5) to (i)(4), (5) and (6).

Section 207.3—"General Requirements", is amended by adding a new paragraph (q).

Section 220.2—"Definitions", is amended by inserting a new item in paragraph (o), between the second and third item and numbering the items (o)(1), (2), (3), (4) and (5).

Section 221.2—"Definitions", is amended by adding a new paragraph (h)(3) and renumbering (h)(3), (4) and (5) to (h)(4), (5) and (6).

Section 221.3—"General Requirements", is amended by adding a new paragraph (1).

The amended paragraphs in Regulations G, T and U read as follows:

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

1. Section 207.2—"Definitions", is amended by revising paragraph (i) to read as follows:

##### § 207.2 Definitions

\* \* \* \* \*

(i) "Margin stock" means:

- (1) Any equity security registered or having unlisted trading privileges on a national securities exchange;
- (2) Any OTC margin stock;
- (3) Any OTC security designated as qualified for trading in the National Market System under a designation plan approved by the Securities and Exchange Commission (NMS Security);
- (4) Any debt security convertible into

a margin stock or carrying a warrant or right to subscribe to or purchase a margin stock;

(5) Any warrant or right to subscribe to or purchase a margin stock; or  
(6) Any security issued by an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), other than:

(i) A company licensed under the Small Business Investment Company Act of 1958, as amended (15 U.S.C. 661); or

(ii) A company which has at least 95 percent of its assets continuously invested in exempted securities (as defined in 15 U.S.C. 78c(12)).

2. Section 207.3—"General Requirements", is amended by adding a new paragraph (g).

**§ 207.3 General Requirements**

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(q) *Lack of notice of NMS security designation.* Failure to treat an NMS security as a margin stock in connection with an extension of credit shall not be deemed a violation of this part if the designation is made between quarterly publications of the Board's List of OTC Margin Stocks and the lender does not have actual notice of the designation.

**PART 220—CREDIT BY BROKERS AND DEALERS**

1. Section 220.2—"Definitions", is amended by revising paragraph (o) to read as follows:

**§ 220.2 Definitions.**

\* \* \* \* \*

(o) "Margin security" means:

(1) Any registered security;  
(2) Any OTC margin stock;  
(3) Any OTC margin bond;  
(4) Any OTC security designated as qualified for trading in the National Market System under a designation plan approved by the Securities and Exchange Commission (NMS security); or

(5) Any security issued by either an open-end investment company or unit investment trust which is registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8).

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

1. Section 221.2—"Definitions", is amended by revising paragraph (h) to read as follows:

**§ 221.2 Definitions.**

\* \* \* \* \*

(h) "Margin stock" means:

(1) Any equity security registered or having unlisted trading privileges on a national securities exchange;  
(2) Any OTC margin stock;  
(3) Any OTC security designated as qualified for trading in the National Market System under a designation plan approved by the Securities and Exchange Commission (NMS security);

(4) Any debt security convertible into a margin stock or carrying a warrant or right to subscribe to or purchase a margin stock;

(5) Any warrant or right to subscribe to or purchase a margin stock; or

(6) Any security issued by an investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8), other than:

(i) A company licensed under the Small Business Investment Company Act of 1958, as amended (15 U.S.C. 661); or

(ii) A company which has at least 95 percent of its assets continuously invested in exempted securities (as defined in 15 U.S.C. 78c(12)).

2. Section 221.3—"General Requirements", is amended by adding a new paragraph (l).

**§ 221.3 General requirements.**

\* \* \* \* \*

(l) *Lack of notice of NMS security designation.* Failure to treat an NMS security as a margin stock in connection with an extension of credit shall not be deemed a violation of this part if the designation is made between quarterly publications of the Board's List of OTC Margin Stocks and the bank does not have actual notice of the designation.

By order of the Board of Governors of the Federal Reserve System, September 5, 1984.

William W. Wiles,  
*Secretary of the Board.*

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