

**FEDERAL RESERVE BANK
OF NEW YORK**

[Circular No. **9815**
March 19, 1985]

MARGIN REGULATIONS

**— Employee Stock Ownership Plans
— Face-Amount Certificates**

*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 issued for public comment a proposed amendment to Regulation G that would give savings and loan associations and other lenders the same authority as banks to extend credit to employee stock ownership plans.

Comment is requested by April 19.

The Board also adopted a technical amendment to its margin regulations (G and U) to exclude face-amount certificates from the definition of margin security. A face-amount certificate is a security issued by an investment company that is registered under the Investment Company Act of 1940, which promises to pay an investor a fixed sum of money at a fixed future date in return for a designated payment. As permitted by the Investment Company Act, face-amount certificates have built-in credit features. In addition, the Board's final action allows broker-dealers to sell these instruments without being considered in violation of the credit-arranging provision of Regulation T.

Printed on the following pages is the text of the Board's proposal on employee stock ownership plans. Comments thereon should be submitted by April 19, 1985, and may be sent to our Regulations Division.

In addition, enclosed is the text of the technical amendments relating to face-amount certificates, effective April 19, 1985. Comments are also invited on these amendments until April 19, 1985, which may be sent to our Regulations Division.

E. GERALD CORRIGAN,
President.

FEDERAL RESERVE SYSTEM

REGULATION G

(12 CFR 207)

[Docket No. R-0529]

SECURITIES CREDIT BY PERSONS OTHER THAN BANKS, BROKERS, OR DEALERS

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed Rule.

SUMMARY: The Board proposes to amend its Regulation G (12 CFR 207) to permit non-bank, non-broker lenders to extend credit to trusts for employee stock option plans (ESOPs) qualified under section 401 of the Internal Revenue Code without regard to the credit limitations normally applicable under Regulation G. This will permit savings and loans and other "G-lenders" to extend such credit on margin stock on the same basis as banks are currently allowed to do under a special exemptive provision in Regulation U. The Board is seeking specific public comment on the question of whether Regulation T (12 CFR 220) should also be amended to provide a comparable provision for brokers and dealers who may wish to lend to ESOPs.

DATE: Comments should be received by April 19, 1985.

ADDRESS: Comments, which should refer to Docket No. R-0529, may be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551, or delivered to Room B-2223 between 8:45 a.m. and 5:15 p.m. weekdays. Comments received may be inspected in Room B-1122 between 8:45 a.m. and 5:15 p.m. weekdays.

FOR FURTHER INFORMATION CONTACT: Laura Homer, Securities Credit Officer, or Robert Lord, Senior Attorney, Division of Banking Supervision and Regulation, (202) 452-2781.

SUPPLEMENTARY INFORMATION: The Board was recently asked by the Federal Reserve Bank of San Francisco to amend Regulation G to permit G-lenders to extend credit to trusts for ESOPs on the same basis as banks. Banks are currently permitted to extend such credit without regard to the credit limitations of Regulation U. For savings and loan associations and other lenders subject to Regulation G, however, there is no comparable exemption. Since an increasing number of savings and loans may want to make such loans, if permitted, and since there is no reason to treat them differently from banks in this area, the Board proposes to extend that lending authority to savings and loan associations as well as other lenders subject to Regulation G.

INITIAL REGULATORY FLEXIBILITY ANALYSIS:

The Board's proposal to amend Regulation G to permit G-lenders to extend, on an exempt basis, credit to ESOPs is not expected to have any adverse impact on a substantial number of small businesses.

List of Subjects in 12 CFR 207

Banks, Banking, Credit, Federal Reserve System, Margin, Margin Requirements, Reporting and Recordkeeping Requirements, Securities.

Accordingly, pursuant to §§ 7 and 23 of the Securities Exchange Act of 1934, as amended (15 U.S.C. §§ 78g and 78w), the Board amends Regulation G in the following manner:

The heading is amended and a new paragraph is added to section 207.5 as follows:

Section 207.5 - Employee Stock Option, Purchase and Ownership Plans

* * * * *

(c) Credit to ESOPs

A lender may extend and maintain purpose credit without regard to the provisions of this part, except for sections 207.3(a) and 207.3(o), if such credit is extended to an employee stock ownership plan (ESOP) qualified under section 401 of the Internal Revenue Code, as amended (26 U.S.C. § 401).

By order of the Board of Governors of the Federal Reserve System,
March 13, 1985.

(signed) William W. Wiles

William W. Wiles
Secretary of the Board

Board of Governors of the Federal Reserve System

SECURITIES CREDIT TRANSACTIONS

AMENDMENTS TO REGULATIONS G, T, AND U

(effective April 19, 1985)

Amendment to margin regulations excluding face-amount certificates from the definition of margin security and permitting broker-dealers to sell them without violating the arranging prohibition of Regulation T

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final Rule.

SUMMARY: The Board is amending: (1) the definition of "margin stock" in Regulations G and U so as to make it clear that the definition does not include face-amount certificates as defined in 15 U.S.C. 80a-2(a)(15), and (2) the "arranging" provision of Regulation T to reflect that a broker-dealer selling these instruments would not be considered to be violating that provision. Although the changes are being made effective April 19, 1985, comments will be received until that date and appropriate modifications, if any, will be made in response to comments.

EFFECTIVE DATE: April 19, 1985.

ADDRESS: Comments, which should refer to Docket No. R-0543, may be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th and Constitution Avenue, N.W., Washington, D.C. 20551, or delivered to Room B-2223 between 8:45 a.m. and 5:15 p.m. weekdays. Comments received may be inspected in Room B-1122 between 8:45 a.m. and 5:15 p.m. weekdays.

FOR FURTHER INFORMATION CONTACT: Laura Homer, Securities Credit Officer, or Douglas Blass, Attorney, Division of Banking Supervision and Regulation, (202) 452-2781.

SUPPLEMENTARY INFORMATION: When the Board recently amended and revised the margin regulations, the definition of "margin stock" in Regulation G (12 CFR 207.2(i)) and Regulation U (12 CFR 221.2(h)) were not revised to exclude face-amount certificates as defined in 15 U.S.C. 80a-2(a)(18), although the revised definition of "margin security" in Regulation T (12 CFR 220.2(o)) did not cover such instruments. Noting these differences, some concern arose in the investment community as to whether companies issuing these certificates were required to register as G-lenders since these certificates have built-in credit features covered by the Investment Company Act of 1940 (15 U.S.C. §§ 80a-1 through 80a-64). Further concern was raised since broker-dealers selling these certificates could be deemed to be in technical violation of the "arranging" provision of Regulation T (12 CFR 220.13). The Board is adopting the proposed amendments to alleviate these concerns.

The Board is taking this action to relieve an unintended restriction and it is believed that it will have no adverse impact upon any member of the public. Because this is a rule change which relieves a restriction, the requirements of the Administrative Procedure Act (5 U.S.C. § 553) with respect to notice and public participation were not followed before adoption. The public is, however, invited to submit comments relating to the adoption of the amendments.

FINAL REGULATORY FLEXIBILITY ANALYSIS:

The Board's action in adopting these amendments is not expected to have any adverse impact on a substantial number of small businesses.

List of Subjects in 12 CFR Part 207

Banks, Banking, Credit, Federal Reserve System,

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) Amendments effective November 13, 1984.
- 4) This slip sheet.

Margin, Margin Requirements, Reporting and Record-keeping Requirements, Securities.

List of Subjects in 12 CFR Part 220

Banks, Banking, Brokers, Credit, Federal Reserve System, Margin, Margin Requirements, Investments, Reporting and Recordkeeping Requirements, Securities.

List of Subjects in 12 CFR Part 221

Banks, Banking, Credit, Federal Reserve System, Margin, Margin Requirements, Reporting and Record-keeping Requirements, Securities.

Accordingly, pursuant to §§ 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 by excluding face-amount certificates from the definition of "margin security" in Regulation G and U and excluding loans on face-amount certificates from prohibited credit arrangements in Regulation T. The amended Regulations G, T and U will read as follows:

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

* * *

SECTION 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(a)(12)); or

(iii) a company which issues face-amount certificates as defined in 15 U.S.C. 80a-2(a)(15), but only with respect to such securities.

PART 220 — CREDIT BY BROKERS AND DEALERS

* * *

SECTION 220.13 — Arranging for Loans by Others

A creditor may not arrange for the extension or maintenance of credit to or for any customer by any person upon terms and conditions other than those upon which the creditor may itself extend or maintain credit under the provisions of this part, except that this limitation shall not apply to credit arranged for a customer which does not violate parts 207 and 221 of this chapter and results solely from:

(a) investment banking services, provided by the creditor to the customer, including, but not limited to, underwritings, private placements, and advice and other services in connection with exchange offers, mergers, or acquisitions, except for underwritings that involve the public distribution of an equity security with installment or other deferred payment provisions; or

(b) the sales of nonmargin securities (including securities with installment or other deferred payment provisions) if the sale is exempted from the registration requirements of the Securities Act of 1933 under section 4(2) or section 4(6) of the act; or

(c) a subsequent loan or advance on a face-amount certificate as permitted under 15 U.S.C. 80a-28(d).

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

* * *

SECTION 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(a)(12)); or

(iii) a company which issues face-amount certificates as defined in 15 U.S.C. 80a-2(a)(15), but only with respect to such securities.

By order of the Board of Governors of the Federal Reserve System, March 13, 1985.

/s/ WILLIAM W. WILES

William W. Wiles
Secretary of the Board