

FEDERAL RESERVE BANK
OF NEW YORK

Circular No. 6328
May 1, 1969

MARGIN REGULATIONS
Interpretation of Regulations G and U

To All Banking Institutions, and Others Concerned,
in the Second Federal Reserve District:

Printed below is an excerpt from the Federal Register of April 29, containing the text of an interpretation of margin Regulations G and U of the Board of Governors of the Federal Reserve System. The interpretation concerns the applicability of the regulations to the guaranty by a corporation of an "unsecured" bank loan to exercise an option to purchase stock of the corporation.

Additional copies of this circular will be furnished upon request.

Alfred Hayes,
President.

Title 12—BANKS AND BANKING

Chapter II—Federal Reserve System

**SUBCHAPTER A—BOARD OF GOVERNORS OF
THE FEDERAL RESERVE SYSTEM**

[Reg. G]

**PART 207—CREDIT BY PERSONS
OTHER THAN BANKS, BROKERS, OR
DEALERS FOR PURPOSE OF PUR-
CHASING OR CARRYING REGIS-
TERED EQUITY SECURITIES**

Guaranty as Extension of Credit

**§ 207.103 Corporate guaranty of bank
loan as extension of credit in the
ordinary course of business.**

(a) The Board recently considered the questions whether (1) the guaranty by a corporation of an "unsecured" bank loan to exercise an option to purchase stock of the corporation is an "extension of credit" for the purpose of this part (Regulation G), (2) such a guaranty is given "in the ordinary course of business" of the corporation, as defined in § 207.2(b), and (3) the bank involved took part in arranging for such credit on better terms than it could extend under the provisions of Part 221 (Regulation U) of this subchapter.

(b) The Board understood that any officer or employee included under the corporation's stock option plan who wished to exercise his option could obtain a loan for the purchase price of the stock by executing an unsecured note to the bank. The corporation would issue to the bank a guaranty of the loan and hold the purchased shares as collateral to secure it against loss on the guaranty. Stock of the corporation is registered on a national securities exchange.

(c) A lender is subject to the registration and other requirements of this part if, in the ordinary course of his business, he extends credit on collateral that includes any registered equity securities in the amount of \$50,000 or more in any calendar quarter, or has such credit outstanding in any calendar quarter in the amount of \$100,000 or more. The Board understood that the corporation in ques-

tion had \$100,000 in guaranties outstanding during the applicable calendar quarter.

(d) In the Board's judgment a person who guarantees a loan, and thereby becomes liable for the amount of the loan in the event the borrower should default, is lending his credit to the borrower. In the circumstances described, such a lending of credit must be considered an "extension of credit" under this part in order to prevent circumvention of the regulation's limitation on the amount of credit that can be extended on the security of registered stock.

(e) Under § 207.2(b), "the term in the ordinary course of his business" means * * * in the case of a person other than an individual, carrying out or in furtherance of any business purpose." In general, stock option plans are designed to provide a company's employees with a proprietary interest in the company in the form of ownership of the company's stock. Such plans increase the company's ability to attract and retain able personnel and, accordingly, promote the interest of the company and its stockholders, while at the same time providing the company's employees with additional incentive to work toward the company's future success. An arrangement whereby participating employees may finance the exercise of their options through an unsecured bank loan guaranteed by the company, thereby facilitating the employees' acquisition of company stock, is likewise designed to promote the company's interest and is, therefore, in furtherance of a business purpose.

(f) For the reasons indicated, the Board concluded that under the circumstances described a guaranty by the corporation constitutes credit extended in the ordinary course of business under this part, that the corporation is required to register pursuant to § 207.2(a), and that such guaranties may not be given in excess of the maximum loan value of the collateral pledged to secure the guaranty, which is 20 percent under the current supplement to this part.

(g) Section 221.3(u) of this subchapter provides that "no bank shall arrange

for the extension or maintenance of any credit for the purpose of purchasing or carrying any stock registered on a national securities exchange, except upon the same terms and conditions on which the bank itself could extend or maintain this credit" under the provisions of Part 221. Since the Board concluded that the giving of a guaranty by the corporation to secure the loan described above constitutes an extension of credit, and since the use of a guaranty in the manner described could not be effectuated without the concurrence of the bank involved, the Board further concluded that the bank took part in "arranging" for the extension of credit in excess of the maximum loan value of the stock pledged to secure the guaranties.

(15 U.S.C. 78g. Interprets or applies 15 U.S.C. 78g(d))

Dated at Washington D.C., this 21st day of April 1969.

By order of the Board of Governors.

[SEAL] ROBERT P. FORRESTAL,
Assistant Secretary.

[F.B. Doc. 69-5020; Filed, Apr. 28, 1969;
8:45 a.m.]

[Reg. U]

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

Arranging for Extension of Credit

**§ 221.118 Bank arranging for extension
of credit by corporation.**

For text of this interpretation, see § 207.103 of this subchapter.

(15 U.S.C. 78g. Interprets or applies 15 U.S.C. 78g(d))

Dated at Washington, D.C., the 21st day of April 1969.

By order of the Board of Governors.

[SEAL] ROBERT P. FORRESTAL,
Assistant Secretary.

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