

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 question 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 §207.1(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.

[34 FR 7005, Apr. 29, 1969; 34 FR 8351, May 30, 1969]

**§207.104 Contribution to joint venture as extension of credit when the contribution is disproportionate to the contributor's share in the venture's profits or losses.**

(a) The Board recently considered the question whether a joint venture, structured so that the amount of capital contribution to the venture would be disproportionate to the right of participation in profits or losses, constitutes an "extension of credit" for the purpose of Regulation G.

(b) An individual and a corporation plan to establish a joint venture to engage in the business of buying and selling securities, including registered equity securities. The individual would contribute 20 percent of the capital and

receive 80 percent of the profits or losses; the corporate share would be the reverse. In computing profits or losses, each participant would first receive interest at the rate of 8 percent on his respective capital contribution. Although purchases and sales would be mutually agreed upon, the corporation could liquidate the joint portfolio if the individual's share of the losses equaled or exceeded his 20 percent contribution to the venture. The corporation would hold the securities, and upon termination of the venture, the assets would first be applied to repayment of capital contributions.

(c) In general, the relationship of joint venture is created when two or more persons combine their money, property, or time in the conduct of some particular line of trade or some particular business and agree to share jointly, or in proportion to capital contributed, the profits and losses of the undertaking.

(d) The incidents of the joint venture described above, however, closely parallel those of an extension of margin credit, with the corporation as lender and the individual as borrower. The corporation supplies 80 percent of the purchase price of securities in exchange for a net return of 8 percent of the amount advanced plus 20 percent of any gain. Like a lender of securities credit, the corporation is insulated against loss by retaining the right to liquidate the collateral before the securities decline in price below the amount of its contribution. Conversely, the individual—like a customer who borrows to purchase securities—puts up only 20 percent of their cost, is entitled to the principal portion of any appreciation in their value, bears the principal risk of loss should that value decline, and does not stand to gain or lose except through a change in value of the securities purchased.

(e) The Board is of the opinion that where the right of an individual to share in profits and losses of such a joint venture is disproportionate to his contribution to the venture:

(1) The joint venture involves an extension of credit by the corporation to the individual;

(2) The extension of credit is to purchase or carry registered equity securi-

ties, and is collateralized by such securities; and

(3) If the corporation is neither a bank subject to Regulation U nor a broker or dealer subject to Regulation T, the credit is of the kind described by § 207.1(a) of Regulation G.

[34 FR 9121, June 10, 1969]

**§ 207.105 Applicability of plan-lender provisions to financing of stock options and stock purchase rights qualified or restricted under Internal Revenue Code.**

(a) The Board has recently been asked whether the plan-lender provisions of § 207.4(a) of Regulation G, "Securities Credit by Persons other than Banks, Brokers, or Dealers," were intended to apply to the financing of stock options restricted or qualified under the Internal Revenue Code where such options or the option plan do not provide for such financing.

(b) Section 207.4(a) of Regulation G permits a corporation or its plan-lender to extend credit to its employees without regard to the normal credit limitations of the regulation for the purpose of exercising stock options or stock purchase rights if the plan or agreement under which the credit is extended complies with certain requirements. Paragraph (1) of § 207.4(a) is in effect a "grandfather clause," exempting from most of the credit limitations of Regulation G any such credit extended in connection with options or rights meeting certain specified "pre-existing" conditions. Generally, these conditions recognize inequities that would result from application of the regulation's restrictions to credit extended in connection with options or rights granted, or contractual commitments made prior to February 1, 1968, the date the adoption of Regulation G was announced. Paragraph (2) of § 207.4(a) provides a more limited exemption for credit extended in connection with options or rights granted after February 1, 1968, and establishes requirements for plans seeking to qualify for this exemption.

(c) Paragraph (iii) of § 207.4(a)(1), which was added effective July 8, 1969, was designed to provide exemption, from all but certain reporting provisions, for credit extended pursuant to