

not permit any withdrawals or substitutions of collateral that would increase such excess; nor could the bank increase the amount of the loan balance unless there was provided additional collateral having a maximum loan value at least equal to the amount of the increase. In other words, as from the date the stock should become registered, the loan would be subject to this part in exactly the same way, for example, as a loan subject to this part that became under-margined because of a decline in the current market value of the loan collateral or because of a decrease by the Board in the maximum loan value of the loan collateral.

[21 FR 1094, Feb. 17, 1956]

**§ 221.109 Loan to open-end investment company.**

In response to a question regarding a possible loan by a bank to an open-end investment company that customarily purchases stocks registered on a national securities exchange, the Board stated that in view of the general nature and operations of such a company, any loan by a bank to such a company should be presumed to be subject to this part as a loan for the purpose of purchasing or carrying registered stocks. This would not be altered by the fact that the open-end company had used, or proposed to use, its own funds or proceeds of the loan to redeem some of its own shares, since mere application of the proceeds of a loan to some other use cannot prevent the ultimate purpose of a loan from being to purchase or carry registered stocks.

[23 FR 8945, Nov. 18, 1958]

**§ 221.110 Questions arising under Regulation U.**

(a) Regulation U governs “any loan” made by a bank “secured directly or indirectly by any stock for the purpose of purchasing or carrying any stock registered on a national securities exchange”, with certain exceptions, and provides that the maximum loan value of such stock shall be a fixed percentage “of its current market value, as determined by any reasonable method.”

(b) The Board of Governors has recently had occasion to consider the ap-

plication of this language to the three following questions:

(1) *Loan secured by stock.* First, is a loan to purchase or carry registered stock subject to Regulation U where made in unsecured form, if stock is subsequently deposited as security with the lending bank, and surrounding circumstances indicate that the parties originally contemplated that the loan should be so secured? The Board answered that in a case of this kind, the loan would be subject to the Regulation, for the following reasons.

(i) The Board has long held, in the closely related *purpose* area, that the original purpose of a loan should not be determined upon a narrow analysis of the technical circumstances under which a loan is made. Instead, the fundamental purpose of the loan is considered to be controlling. Indeed, “the fact that a loan made on the borrower’s signature only, for example, becomes secured by registered stock shortly after the disbursement of the loan” affords reasonable grounds for questioning whether the bank was entitled to rely upon the borrower’s statement as to the purpose of the loan. 1953 Bull. 951.

(ii) Where security is involved, standards of interpretation should be equally searching. If, for example, the original agreement between borrower and bank contemplated that the loan should be secured by registered stock, and such stock is in fact delivered to the bank when available, the transaction must be regarded as fundamentally a secured loan. This view is strengthened by the fact that the regulation applies to a loan “secured directly or indirectly by any stock.”

(2) *Loan to acquire controlling shares.*

(i) The second question is whether the Regulation governs a stock-secured loan made for the business purpose of purchasing a controlling interest in a corporation, or whether such a loan would be exempt on the ground that the Regulation is directed solely toward purchases of stock for speculative or investment purposes. The Board answered that a stock-secured loan for the purpose of purchasing or carrying registered stock is subject to the Regulation, regardless of the reason for which the purchase is made.