

§ 221.114 Bank loans to purchase stock of American Telephone and Telegraph Company under Employees' Stock Plan.

(a) The Board of Governors recently interpreted Part 221 (Regulation U) in connection with proposed loans by a bank to persons who are purchasing shares of stock of American Telephone and Telegraph Company pursuant to its Employees' Stock Plan.

(b) According to the current offering under the Plan, an employee of the AT&T system may purchase shares through regular deductions from his pay over a period of 24 months. At the end of that period, a certificate for the appropriate number of shares will be issued to the participating employee by AT&T. Each employee is entitled to purchase, as a maximum, shares that will cost him approximately three-fourths of his annual base pay. Since the program extends over two years, it follows that the payroll deductions for this purpose may be in the neighborhood of 38 percent of base pay and a larger percentage of "take-home pay." Deductions of this magnitude are in excess of the saving rate of many employees.

(c) Certain AT&T employees, who wish to take advantage of the current offering under the Plan, are the owners of shares of AT&T stock that they purchased under previous offerings. A bank proposed to receive such stock as collateral for a "living expenses" loan that will be advanced to the employee in monthly installments over the 24-month period, each installment being in the amount of the employee's monthly payroll deduction under the Plan. The aggregate amount of the advances over the 24-month period would be substantially greater than the maximum loan value of the collateral as prescribed in § 221.4, the Supplement to Regulation U (30 percent, at the present time).

(d) In the opinion of the Board of Governors, a loan of the kind described would violate this part 221 if it exceeded the maximum loan value of the collateral. The regulation applies to any stock-secured loan for the purpose of purchasing or carrying stock registered on a national securities exchange (§ 221.1(a)). Although the proposed loan

would purport to be for living expenses, it seems quite clear, in view of the relationship of the loan to the Employees' Stock Plan, that its actual purpose would be to enable the borrower to purchase AT&T stock, which is registered on a national securities exchange. At the end of the 24-month period the borrower would acquire a certain number of shares of that stock and would be indebted to the lending bank in an amount approximately equal to the amount he would pay for such shares. In these circumstances, the loan by the bank must be regarded as a loan "for the purpose of purchasing" the stock, and therefore it is subject to the limitations prescribed by this part 221. This conclusion follows from the provisions of the part, and it may also be observed that a contrary conclusion could largely defeat the basic purpose of the margin regulations.

(e) Accordingly, the Board concluded that a loan of the kind described may not be made in an amount exceeding the maximum loan value of the collateral, as prescribed by the current Supplement to Regulation U (§ 221.4).

[27 FR 5538, June 12, 1962]

§ 221.115 Accepting a purpose statement through the mail without benefit of face-to-face interview.

For text of an interpretation on this subject, see § 207.110 of this subchapter (15 U.S.C. 78g).

[43 FR 30039, July 13, 1978]

§ 221.116 Bank loans to replenish working capital used to purchase mutual fund shares.

(a) In a situation recently considered by the Board of Governors, a business concern ("X") proposed to purchase mutual fund shares, from time to time, with proceeds from its accounts receivable, then pledge the shares with a bank in order to secure working capital. The bank was prepared to lend amounts equal to 70 percent of the current value of the shares as they were purchased by X. If the loans were subject to this part (Regulation U), only 30 percent of the current market value of the shares could be lent.

(b) The immediate purpose of the loans would be to replenish X's working capital. However, as time went on,

X would be acquiring mutual fund shares at a cost that would exceed the net earnings it would normally have accumulated, and would become indebted to the lending bank in an amount approximately 70 percent of the prices of said shares.

(c) The Board held that the loans were for the purpose of purchasing the shares, and therefore subject to the limitations prescribed by this part. As pointed out in §221.114 with respect to a similar program for putting a high proportion of cash income into stock, then borrowing against the stock to meet needs for which the cash would otherwise have been required, a contrary conclusion could largely defeat the basic purpose of the margin regulations.

(d) Also considered was an alternative proposal under which X would deposit proceeds from accounts receivable in a time account for 1 year, before using those funds to purchase mutual fund shares. The Board held that this procedure would not change the situation in any significant way. Once the arrangement was established, the proceeds would be flowing into the time account at the same time that similar amounts were released to purchase the shares, and over any extended period of time the result would be the same. Accordingly, the Board concluded that bank loans made under the alternative proposal would similarly be subject to this part.

[32 FR 8357, June 10, 1967]

§221.117 When bank in “good faith” has not relied on stock as collateral.

(a) The Board has received questions regarding the circumstances in which an extension or maintenance of credit will not be deemed to be “indirectly secured” by stock as indicated by the phrase, “if the bank in good faith has not relied upon such stock as collateral,” contained in clause (2) of a recent amendment to §221.3(c) of Regulation U. A similar phrase is contained in §207.2(g) of Regulation G of this chapter and the following applies to that paragraph, insofar as appropriate and consistent.

(b) In response, the Board noted that in amending this portion of the regulation it was indicated that one of the

purposes of the change was to make clear that §221.3(c) does not apply to certain routine negative covenants in loan agreements. Also, while the question of whether or not a bank has relied upon particular stock as collateral is necessarily a question of fact to be determined in each case in the light of all relevant circumstances, some indication that the bank had not relied upon stock as collateral would seem to be afforded by such circumstances as the fact that (1) the bank had obtained a reasonably current financial statement of the borrower and this statement could reasonably support the loan, and (2) the loan was not payable on demand or because of fluctuations in market value of the stock, but instead was payable on one or more fixed maturities which were typical of maturities applied by the bank to loans otherwise similar except for not involving any possible question of stock collateral.

[33 FR 7485, May 21, 1968]

§221.118 Bank arranging for extension of credit by corporation.

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

[34 FR 7005, Apr. 29, 1969]

§221.119 Status after July 8, 1969, of credit extended prior to that date to purchase or carry mutual fund shares.

(a) Prior to July 8, 1969, the margin and other requirements of Regulations G and U applied to credit extended to purchase or carry shares of a mutual fund (secured by certain described collateral), if (1) the portfolio of the fund did “customarily include” securities that would themselves have been subject to the regulations and (2) the fund was included in a list of such funds that the Board published for this purpose.

(b) It was found that virtually all mutual funds met the “customarily include” test. Accordingly, for administrative reasons, the Board discontinued publication of the list and restated the rule to cover all mutual funds except those at least 95 percent of whose assets are continuously invested in exempted securities.