

**PART 221— CREDIT BY BANKS AND PERSONS OTHER THAN BROKERS OR DEALERS FOR THE PURPOSE OF PURCHASING OR CARRYING MARGIN STOCK (REGULATION U)**

Sec.

221.1 Authority, purpose, and scope.

221.2 Definitions.

221.3 General requirements.

221.4 Employee stock option, purchase, and ownership plans.

221.5 Special purpose loans to brokers and dealers.

221.6 Exempted transactions.

221.7 Supplement: Maximum loan value of margin stock and other collateral.

finance corporate takeovers.

221.125 Credit to brokers and dealers.

Authority: 15 U.S.C. 78c, 78g, 78q, and 78w.

**§ 221.1 Authority, purpose, and scope.**

(a) Authority. Regulation U (this part) is issued by the Board of Governors of the Federal Reserve System (the Board) pursuant to the Securities Exchange Act of 1934 (the Act) (15 U.S.C. 78a et seq.).

(b) Purpose and scope. (1) This part imposes credit restrictions upon persons other than brokers or dealers

(hereinafter lenders) that extend credit

for the purpose of buying or carrying margin stock if the credit is secured directly or indirectly by margin stock.

Lenders include “banks” (as defined in § 221.2) and other persons who are

required to register with the Board under § 221.3(b). Lenders may not

extend more than the maximum loan

value of the collateral securing such credit, as set by the Board in § 221.7 (the

Supplement).

(2) This part does not apply to clearing agencies regulated by the Securities and Exchange Commission or the Commodity Futures Trading Commission that accept deposits of margin stock in connection with:

(i) The issuance of, or guarantee of, or the clearance of transactions in, any security (including options on any security, certificate of deposit, securities index or foreign currency); or

(ii) The guarantee of contracts for the purchase or sale of a commodity for future delivery or options on such contracts.

(3) This part does not apply to credit extended to an exempted borrower.

(c) Availability of forms. The forms referenced in this part are available from the Federal Reserve Banks.

**§ 221.2 Definitions.**

The terms used in this part have the meanings given them in section 3(a) of

the Act or as defined in this section as follows:

Affiliate means:

(1) For banks:

(i) Any bank holding company of which a bank is a subsidiary within the meaning of the Bank Holding Company Act of 1956, as amended (12 U.S.C. 1841(d));

(ii) Any other subsidiary of such bank holding company; and

(iii) Any other corporation, business trust, association, or other similar organization that is an affiliate as defined in section 2(b) of the Banking Act of 1933 (12 U.S.C. 221a(c));

(2) For nonbank lenders, affiliate means any person who, directly or indirectly, through one or more intermediaries, controls, or is controlled by, or is under common control with the lender.

Bank. (1) Bank. Has the meaning given to it in section 3(a)(6) of the Act (15 U.S.C. 78c(a)(6)) and includes:

(i) Any subsidiary of a bank;

(ii) Any corporation organized under section 25(a) of the Federal Reserve Act (12 U.S.C. 611); and

(iii) Any agency or branch of a foreign bank located within the United States.

(2) Bank does not include:

(i) Any savings and loan association;

(ii) Any credit union;

(iii) Any lending institution that is an instrumentality or agency of the United States; or

(iv) Any member of a national securities exchange.

Carrying credit is credit that enables a customer to maintain, reduce, or retire indebtedness originally incurred to purchase a security that is currently a margin stock.

Current market value of:

(1) A security means:

(i) If quotations are available, the closing sale price of the security on the preceding business day, as appearing on any regularly published reporting or quotation service; or

(ii) If there is no closing sale price, the lender may use any reasonable estimate of the market value of the security as of the close of business on the preceding business day; or

(iii) If the credit is used to finance the purchase of the security, the total cost of purchase, which may include any commissions charged.

(2) Any other collateral means a value determined by any reasonable method.

Customer excludes an exempted

borrower and includes any person or persons acting jointly, to or for whom a lender extends or maintains credit.

Examining authority means:

(1) The national securities exchange or national securities association of which a broker or dealer is a member; or

(2) If a member of more than one self-regulatory organization, the organization designated by the Securities and Exchange Commission as the examining authority for the broker or dealer.

Exempted borrower means a member of a national securities exchange or a registered broker or dealer, a substantial portion of whose business consists of transactions with persons other than brokers or dealers, and includes a borrower who:

(1) Maintains at least 1000 active accounts on an annual basis for persons other than brokers, dealers, and persons associated with a broker or dealer;

(2) Earns at least \$10 million in gross revenues on an annual basis from transactions with persons other than brokers, dealers, and persons associated with a broker or dealer; or

(3) Earns at least 10 percent of its gross revenues on an annual basis from transactions with persons other than brokers, dealers, and persons associated with a broker-dealer.

Good faith with respect to:

(1) The loan value of collateral means that amount (not exceeding 100 per cent of the current market value of the collateral) which a lender, exercising sound credit judgment, would lend, without regard to the customer’s other assets held as collateral in connection with unrelated transactions.

(2) Making a determination or accepting a statement concerning a borrower means that the lender or its duly authorized representative is alert to the circumstances surrounding the credit, and if in possession of information that would cause a prudent person not to make the determination or accept the notice or certification without inquiry, investigates and is satisfied that it is correct;

In the ordinary course of business means occurring or reasonably expected to occur in carrying out or furthering any business purpose, or in the case of an individual, in the course of any activity for profit or the management or preservation of property.

Indirectly secured. (1) Includes any

arrangement with the customer under which:

- (i) The customer's right or ability to sell, pledge, or otherwise dispose of margin stock owned by the customer is in any way restricted while the credit remains outstanding; or
- (ii) The exercise of such right is or may be cause for accelerating the maturity of the credit.

(2) Does not include such an arrangement if:

- (i) After applying the proceeds of the credit, not more than 25 percent of the value (as determined by any reasonable method) of the assets subject to the arrangement is represented by margin stock;
- (ii) It is a lending arrangement that permits accelerating the maturity of the credit as a result of a default or renegotiation of another credit to the customer by another lender that is not an affiliate of the lender;
- (iii) The lender holds the margin stock only in the capacity of custodian, depository, or trustee, or under similar circumstances, and, in good faith, has not relied upon the margin stock as collateral; or
- (iv) The lender, in good faith, has not relied upon the margin stock as collateral in extending or maintaining the particular credit.

Lender means:

- (1) Any bank; or
- (2) Any person subject to the registration requirements of this part.

Margin stock means:

- (1) Any equity security registered or having unlisted trading privileges on a national securities exchange;
- (2) 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);
- (3) Any debt security convertible into a margin stock or carrying a warrant or right to subscribe to or purchase a margin stock;
- (4) Any warrant or right to subscribe to or purchase a margin stock; or
- (5) 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 of such securities; or
- (iv) A company which is considered a money market fund under SEC Rule 2a-7 (17 CFR 270.2a-7).

Maximum loan value is the percentage of current market value assigned by the Board under § 221.7 (the Supplement) to specified types of collateral. The maximum loan value of margin stock is stated as a percentage of its current market value. Puts, calls and combinations thereof that do not qualify as margin stock have no loan value. All other collateral has good faith loan value.

Nonbank lender means any person subject to the registration requirements of this part.

Purpose credit is any credit for the purpose, whether immediate, incidental, or ultimate, of buying or carrying margin stock.

**§ 221.3 General requirements.**

(a) Extending, maintaining, and arranging credit—(1) Extending credit. No lender, except a plan-lender, as defined in § 221.4(a), shall extend any purpose credit, secured directly or indirectly by margin stock, in an amount that exceeds the maximum loan value of the collateral securing the credit.

(2) Maintaining credit. A lender may continue to maintain any credit initially extended in compliance with this part, regardless of:

- (i) Reduction in the customer's equity resulting from change in market prices;
- (ii) Change in the maximum loan value prescribed by this part; or
- (iii) Change in the status of the security (from nonmargin to margin) securing an existing purpose credit.

(3) Arranging credit. No lender may arrange for the extension or maintenance of any purpose credit, except upon the same terms and conditions under which the lender itself may extend or maintain purpose credit under this part.

(b) Registration of nonbank lenders; termination of registration; annual report—(1) Registration. Every person other than a person subject to part 220 of this chapter or a bank who, in the ordinary course of business, extends or maintains credit secured, directly or

indirectly, by any margin stock shall register on Federal Reserve Form FR G-1 (OMB control number 7100-0011) within 30 days after the end of any calendar quarter during which:

- (i) The amount of credit extended equals \$200,000 or more; or
- (ii) The amount of credit outstanding at any time during that calendar quarter equals \$500,000 or more.

(2) Deregistration. A registered nonbank lender may apply to terminate its registration, by filing Federal Reserve Form FR G-2 (OMB control number 7100-0011), if the lender has not, during the preceding six calendar months, had more than \$200,000 of such credit outstanding. Registration shall be deemed terminated when the application is approved by the Board.

(3) Annual report. Every registered nonbank lender shall, within 30 days following June 30 of every year, file Form FR G-4 (OMB control number 7100-0011).

(4) Where to register and file applications and reports. Registration statements, applications to terminate registration, and annual reports shall be filed with the Federal Reserve Bank of the district in which the principal office of the lender is located.

(c) Purpose statement—(1) General rule—(i) Banks. Except for credit extended under paragraph (c)(2) of this section, whenever a bank extends credit secured directly or indirectly by any margin stock, in an amount exceeding \$100,000, the bank shall require its customer to execute Form FR U-1 (OMB No. 7100-0115), which shall be signed and accepted by a duly authorized officer of the bank acting in good faith.

(ii) Nonbank lenders. Except for credit extended under paragraph (c)(2) of this section or § 221.4, whenever a nonbank lender extends credit secured directly or indirectly by any margin stock, the nonbank lender shall require its customer to execute Form FR G-3 (OMB control number 7100-0018), which shall be signed and accepted by a duly authorized representative of the nonbank lender acting in good faith.

(2) Purpose statement for revolving-credit or multiple-draw agreements or financing of securities purchases on a payment-against-delivery basis—(i) Banks. If a bank extends credit, secured directly or indirectly by any margin stock, in an amount exceeding \$100,000, under a revolving-credit or other multiple-draw agreement, Form FR U-1

must be executed at the time the credit arrangement is originally established and must be amended as described in paragraph (c)(2)(iv) of this section for each disbursement if all of the collateral for the agreement is not pledged at the time the agreement is originally established.

(ii) Nonbank lenders. If a nonbank lender extends credit, secured directly or indirectly by any margin stock, under a revolving-credit or other multiple-draw agreement, Form FR G-3 must be executed at the time the credit arrangement is originally established and must be amended as described in paragraph (c)(2)(iv) of this section for each disbursement if all of the collateral for the agreement is not pledged at the time the agreement is originally established.

(iii) Collateral. If a purpose statement executed at the time the credit arrangement is initially made indicates that the purpose is to purchase or carry margin stock, the credit will be deemed in compliance with this part if:

(A) The maximum loan value of the collateral at least equals the aggregate amount of funds actually disbursed; or  
(B) At the end of any day on which credit is extended under the agreement, the lender calls for additional collateral sufficient to bring the credit into compliance with § 221.7 (the Supplement).

(iv) Amendment of purpose statement. For any purpose credit disbursed under the agreement, the lender shall obtain and attach to the executed Form FR U-1 or FR G-3 a current list of collateral which adequately supports all credit extended under the agreement.

(d) Single credit rule. (1) All purpose credit extended to a customer shall be treated as a single credit, and all the collateral securing such credit shall be considered in determining whether or not the credit complies with this part, except that syndicated loans need not be aggregated with other unrelated purpose credit extended by the same lender.

(2) A lender that has extended purpose credit secured by margin stock may not subsequently extend unsecured purpose credit to the same customer unless the combined credit does not exceed the maximum loan value of the collateral securing the prior credit.

(3) If a lender extended unsecured purpose credit to a customer prior to the extension of purpose credit secured by

margin stock, the credits shall be combined and treated as a single credit solely for the purposes of the withdrawal and substitution provision of paragraph (f) of this section.

(4) If a lender extends purpose credit secured by any margin stock and non-purpose credit to the same customer, the lender shall treat the credits as two separate loans and may not rely upon the required collateral securing the purpose credit for the nonpurpose credit.

(e) Exempted borrowers. (1) An exempted borrower that has been in existence for less than one year may meet the definition of exempted borrower based on a six-month period.

(2) Once a member of a national securities exchange or registered broker or dealer ceases to qualify as an exempted borrower, it shall notify its lenders of this fact. Any new extensions of credit to such a borrower, including rollovers, renewals, and additional draws on existing lines of credit, are subject to the provisions of this part.

(f) Withdrawals and substitutions. (1) A lender may permit any withdrawal or substitution of cash or collateral by the customer if the withdrawal or substitution would not:

(i) Cause the credit to exceed the maximum loan value of the collateral; or  
(ii) Increase the amount by which the credit exceeds the maximum loan value of the collateral.

(2) For purposes of this section, the maximum loan value of the collateral on the day of the withdrawal or substitution shall be used.

(g) Exchange offers. To enable a customer to participate in a reorganization, recapitalization or exchange offer that is made to holders of an issue of margin stock, a lender may permit substitution of the securities received. A nonmargin, nonexempted security acquired in exchange for a margin stock shall be treated as if it is margin stock for a period of 60 days following the exchange.

(h) Renewals and extensions of maturity. A renewal or extension of maturity of a credit need not be considered a new extension of credit if the amount of the credit is increased only by the addition of interest, service charges, or taxes with respect to the credit.

(i) Transfers of credit. (1) A transfer of a credit between customers or between

lenders shall not be considered a new extension of credit if:

(i) The original credit was extended by a lender in compliance with this part or by a lender subject to part 207 of this chapter in effect prior to April 1, 1998, (See part 207 appearing in the 12 CFR parts 200 to 219 edition revised as of January 1, 1997), in a manner that would have complied with this part;  
(ii) The transfer is not made to evade this part;  
(iii) The amount of credit is not increased; and  
(iv) The collateral for the credit is not changed.

(2) Any transfer between customers at the same lender shall be accompanied by a statement by the transferor customer describing the circumstances giving rise to the transfer and shall be accepted and signed by a representative of the lender acting in good faith. The lender shall keep such statement with its records of the transferee account.

(3) When a transfer is made between lenders, the transferee shall obtain a copy of the Form FR U-1 or Form FR G-3 originally filed with the transferor and retain the copy with its records of the transferee account. If no form was originally filed with the transferor, the transferee may accept in good faith a statement from the transferor describing the purpose of the loan and the collateral securing it.

(j) Action for lender's protection. Nothing in this part shall require a bank to waive or forego any lien or prevent a bank from taking any action it deems necessary in good faith for its protection.

(k) Mistakes in good faith. A mistake in good faith in connection with the extension or maintenance of credit shall not be a violation of this part.

**§ 221.4 Employee stock option, purchase, and ownership plans.**

(a) Plan-lender; eligible plan. (1) Plan-lender means any corporation, (including a wholly-owned subsidiary, or a lender that is a thrift organization whose membership is limited to employees and former employees of the corporation, its subsidiaries or affiliates) that extends or maintains credit to finance the acquisition of margin stock of the corporation, its subsidiaries or affiliates under an eligible plan.  
(2) Eligible plan. An eligible plan means any employee stock option, purchase, or ownership plan adopted by

a corporation and approved by its stockholders that provides for the purchase of margin stock of the corporation, its subsidiaries, or affiliates.

(b) Credit to exercise rights under or finance an eligible plan. (1) If a plan-lender extends or maintains credit under an eligible plan, any margin stock that directly or indirectly secured that credit shall have good faith loan value. (2) Credit extended under this section shall be treated separately from credit extended under any other section of this part except § 221.3(b)(1) and (b)(3). (c) Credit to ESOPs. A nonbank lender may extend and maintain purpose credit without regard to the provisions of this part, except for § 221.3(b)(1) and (b)(3), 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).

**§ 221.5 Special purpose loans to brokers and dealers.**

(a) Special purpose loans. A lender may extend and maintain purpose credit to brokers and dealers without regard to the limitations set forth in §§ 221.3 and 221.7, if the credit is for any of the specific purposes and meets the conditions set forth in paragraph (c) of this section.

(b) Written notice. Prior to extending credit for more than a day under this section, the lender shall obtain and accept in good faith a written notice or certification from the borrower as to the purposes of the loan. The written notice or certification shall be evidence of continued eligibility for the special credit provisions until the borrower notifies the lender that it is no longer eligible or the lender has information that would cause a reasonable person to question whether the credit is being used for the purpose specified.

(c) Types of special purpose credit. The types of credit that may be extended and maintained on a good faith basis are as follows:

(1) Hypothecation loans. Credit secured by hypothecated customer securities that, according to written notice received from the broker or dealer, may be hypothecated by the broker or dealer under Securities and Exchange Commission (SEC) rules.

(2) Temporary advances in payment-against-delivery transactions. Credit to

finance the purchase or sale of securities for prompt delivery, if the credit is to be repaid upon completion of the transaction.

(3) Loans for securities in transit or transfer. Credit to finance securities in transit or surrendered for transfer, if the credit is to be repaid upon completion of the transaction.

(4) Intra-day loans. Credit to enable a broker or dealer to pay for securities, if the credit is to be repaid on the same day it is extended.

(5) Arbitrage loans. Credit to finance proprietary or customer bona fide arbitrage transactions. For the purpose of this section bona fide arbitrage means:

(i) Purchase or sale of a security in one market, together with an offsetting sale or purchase of the same security in a different market at nearly the same time as practicable, for the purpose of taking advantage of a difference in prices in the two markets; or

(ii) Purchase of a security that is, without restriction other than the payment of money, exchangeable or convertible within 90 calendar days of the purchase into a second security, together with an offsetting sale of the second security at or about the same time, for the purpose of taking advantage of a concurrent disparity in the price of the two securities.

(6) Market maker and specialist loans. Credit to a member of a national securities exchange or registered broker or dealer to finance its activities as a market maker or specialist.

(7) Underwriter loans. Credit to a member of a national securities exchange or registered broker or dealer to finance its activities as an underwriter.

(8) Emergency loans. Credit that is essential to meet emergency needs of the broker-dealer business arising from exceptional circumstances.

(9) Capital contribution loans. Capital contribution loans include:

(i) Credit that Board has exempted by order upon a finding that the exemption is necessary or appropriate in the public interest or for the protection of investors, provided the Securities Investor Protection Corporation certifies to the Board that the exemption is appropriate; or

(ii) Credit to a customer for the purpose of making a subordinated loan or capital contribution to a broker or dealer in conformity with the SEC's net

capital rules and the rules of the broker's or dealer's examining authority, provided:

(A) The customer reduces the credit by the amount of any reduction in the loan or contribution to the broker or dealer; and

(B) The credit is not used to purchase securities issued by the broker or dealer in a public distribution.

(10) Credit to clearing brokers or dealers. Credit to a member of a national securities exchange or registered broker or dealer whose nonproprietary business is limited to financing and carrying the accounts of registered market makers.

**§ 221.6 Exempted transactions.**

A bank may extend and maintain purpose credit without regard to the provisions of this part if such credit is extended:

(a) To any bank;

(b) To any foreign banking institution;

(c) Outside the United States;

(d) To an employee stock ownership plan (ESOP) qualified under section 401 of the Internal Revenue Code (26 U.S.C. 401);

(e) To any plan lender as defined in § 221.4(a) to finance an eligible plan as defined in § 221.4(b), provided the bank has no recourse to any securities purchased pursuant to the plan;

(f) To any customer, other than a broker or dealer, to temporarily finance the purchase or sale of securities for prompt delivery, if the credit is to be repaid in the ordinary course of business upon completion of the transaction and is not extended to enable the customer to pay for securities purchased in an account subject to part 220 of this chapter;

(g) Against securities in transit, if the credit is not extended to enable the customer to pay for securities purchased in an account subject to part 220 of this chapter; or

(h) To enable a customer to meet emergency expenses not reasonably foreseeable, and if the extension of credit is supported by a statement executed by the customer and accepted and signed by an officer of the bank acting in good faith. For this purpose, emergency expenses include expenses arising from circumstances such as the death or disability of the customer, or some other change in circumstances involving extreme hardship, not reasonably foreseeable at the time the credit was extended. The opportunity to

realize monetary gain or to avoid loss is not a "change in circumstances" for this purpose.

**§ 221.7 Supplement: Maximum loan value of margin stock and other collateral.**

(a) Maximum loan value of margin stock. The maximum loan value of any margin stock is fifty per cent of its current market value.

(b) Maximum loan value of nonmargin stock and all other collateral. The maximum loan value of nonmargin stock and all other collateral except puts, calls, or combinations thereof is their good faith loan value.

(c) Maximum loan value of options. Except for options that qualify as margin stock, puts, calls, and combinations thereof have no loan value.