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mechanics of making the loan, the purpose being to avoid cumbersome procedures.

(c) Loans are secured by the credit balance of the borrowing participants in the savings fund, including stock, but excluding (in practice) insurance and annuity contracts and government securities. Additional stocks may be, but, in practice, have not been pledged as collateral for loans. Loans are not made, under the plan, from bank funds, and participants do not borrow from the bank upon assignment of the participants' accounts in the trust.

(d) It is urged that loans under the plan are not subject to this part because a loan should not be considered as having been made by a bank where the bank acts solely in its capacity of trustee, without exercise of any discretion.

(e) The Board reviewed this question upon at least one other occasion, and full consideration has again been given to the matter. After considering the arguments on both sides, the Board has reaffirmed its earlier view that, in conformity with an interpretation not published in the Code of Federal Regulations which was published at page 874 of the 1946 Federal Reserve Bulletin (*See* 12 CFR 261.10(f) for information on how to obtain Board publications.), this part applies to the activities of a bank when it is acting in its capacity as trustee. Although the bank in that case had at best a limited discretion with respect to loans made by it in its capacity as trustee, the Board concluded that this fact did not affect the application of the regulation to such loans.

§ 221.113 Loan which is secured indirectly by stock.

(a) A question has been presented to the Board as to whether a loan by a bank to a mutual investment fund is ''secured * * * indirectly by margin stock'' within the meaning of § 221.(3)(a), so that the loan should be treated as subject to this part.

(b) Briefly, the facts are as follows. Fund X, an open-end investment company, entered into a loan agreement with Bank Y, which was (and still is) custodian of the securities which comprise the portfolio of Fund X. The agreement includes the following terms, which are material to the question before the Board:

(1) Fund X agrees to have an ''asset coverage'' (as defined in the agreements) of 400 percent of all its borrowings, including the proposed borrowing, at the time when it takes down any part of the loan.

(2) Fund X agrees to maintain an ''asset coverage'' of at least 300 percent of its borrowings at all times.

(3) Fund X agrees not to amend its custody agreement with Bank Y, or to substitute another custodian without Bank Y's consent.

(4) Fund X agrees not to mortgage, pledge, or otherwise encumber any of its assets elsewhere than with Bank Y.

(c) In § 221.109 the Board stated that because of ''the general nature and operations of such a company'', any ''loan by a bank to an open-end investment company that customarily purchases margin stock * * * should be presumed to be subject to this part as a loan for the purpose of purchasing or carrying margin stock'' (purpose credit). The Board's interpretation went on to say that: ''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 * * *.''

(d) Accordingly, the loan by Bank Y to Fund X was and is a ''purpose credit''. However, a loan by a bank is not subject to this part unless: it is a purpose credit; and it is ''secured directly or indirectly by margin stock''. In the present case, the loan is not ''secured directly'' by stock in the ordinary sense, since the portfolio of Fund X is not pledged to secure the credit from Bank Y. But the word ''indirectly'' must signify some form of security arrangement other than the ''direct'' security which arises from the ordinary ''transaction that gives recourse against a particular chattel or land or against a third party on an obligation'' described in the American Law Institute's Restatement of the Law of Security, page 1. Otherwise the word ''indirectly'' would be superfluous, and a regulation, like a statute, must be construed if possible to give meaning to every word.

(e) The Board has indicated its view that any arrangement under which margin stock is more readily available as security to the lending bank than to other creditors of the borrower may amount to indirect security within the meaning of this part. In an interpretation published at § 221.110 it stated: ''The Board has long held, in the * * * 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 * * * . Where security is involved, standards of interpretation should be equally searching.'' In its pamphlet issued for the benefit and guidance of banks and bank examiners, entitled ''Questions and Answers Illustrating Application of Regulation U'', the Board said: ''In determining whether a loan is ''indirectly'' secured, it should be borne in mind that the reason the Board has thus far refrained * * * from regulating loans not secured by stock has been to simplify operations under the regulation. This objective of simplifying operations does not apply to loans in which arrangements are made to retain the substance of stock collateral while sacrificing only the form''.

(f) A wide variety of arrangements as to collateral can be made between bank and borrower which will serve, to some extent, to protect the interest of the bank in seeing that the loan is repaid, without giving the bank a conventional direct ''security'' interest in the collateral. Among such arrangements which have come to the Board's attention are the following:

(1) The borrower may deposit margin stock in the custody of the bank. An arrangement of this kind may not, it is true, place the bank in the position of a secured creditor in case of bankruptcy, or even of conflicting claims, but it is likely effectively to strengthen the bank's position. The definition of *indirectly secured* in § 221.2, which provides that a loan is not indirectly secured if the lender ''holds the margin stock only in the capacity of custodian, depositary or trustee, or under similar circumstances, and, in good faith has not relied upon the margin stock as collateral,'' does not exempt a deposit of this kind from the impact of the regulation unless it is clear that the bank ''has not relied'' upon the margin stock deposited with it.

(2) A borrower may not deposit his margin stock with the bank, but agree not to pledge or encumber his assets elsewhere while the loan is outstanding. Such an agreement may be difficult to police, yet it serves to some extent to protect the interest of the bank if only because the future credit standing and business reputation of the borrower will depend upon his keeping his word. If the assets covered by such an agreement include margin stock, then, the credit is ''indirectly secured'' by the margin stock within the meaning of this part.

(3) The borrower may deposit margin stock with a third party who agrees to hold the stock until the loan has been paid off. Here, even though the parties may purport to provide that the stock is not ''security'' for the loan (for example, by agreeing that the stock may not be sold and the proceeds applied to the debt if the borrower fails to pay), the mere fact that the stock is out of the borrower's control for the duration of the loan serves to some extent to protect the bank.

(g) The three instances described in paragraph (f) of this section are merely illustrative. Other methods, or combinations of methods, may serve a similar purpose. The conclusion that any given arrangement makes a credit ''indirectly secured'' by margin stock may, but need not, be reinforced by facts such as that the stock in question was purchased with proceeds of the loan, that the lender suggests or insists upon the arrangement, or that the loan would probably be subject to criticism by supervisory authorities were it not for the protective arrangement.

(h) Accordingly, the Board concludes that the loan by Bank Y to Fund X is indirectly secured by the portfolio of the fund and must be treated by the bank as a regulated loan.

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

(a) The Board of Governors interpreted this part in connection with proposed loans by a bank to persons who are purchasing shares of stock of