

Compliance

[Load
Table of
Contents](#)

Regulation U

CONFIDENTIAL

[Executive Summary](#)

[Reporting Requirement — Purpose Statement \(Form FR U-1\)](#)

[Collateral Value Requirement — Purpose Credit Secured by Any Margin Stock](#)

[Single Credit Rule](#)

[Account Officer Responsibility](#)

[Examples](#)

Executive Summary

Regulation U prohibits the bank from extending 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.

"Purpose Credit" means any credit for the purpose, whether immediate, incidental, or ultimate, of buying or carrying margin stock. There is no dollar threshold for the collateral requirement - a \$50,000 purpose credit secured by any margin stock is subject to the collateral value requirements even though a purpose statement is not required; however, the records maintained should clearly establish the value of the collateral securing the credit. This is particularly important when a mixed collateral loan is made.

Regulation U has two major requirements:

- A reporting obligation for loans secured by any margin stock
- A maximum loan value requirement on purpose credit loans secured by margin stock.

The collateral value requirement applies regardless of the size of the credit if the credit is a purpose credit secured directly or indirectly by any margin stock. Obtaining a purpose statement is triggered by the amount of all credits (purpose and non-purpose) secured directly or indirectly by any margin stock. At CTX, a Form FR U-1 is obtained for all stock-secured loans.

Reporting Requirement — Purpose Statement (Form FR U-1)

The customer must execute a Purpose Statement (Form FR U-1) whenever the bank extends credit secured directly or indirectly by any margin stock in an amount exceeding \$100,000. In determining whether the \$100,000 threshold is met, the lender must aggregate all loans to the customer secured directly or indirectly by any margin stock.

"Margin Stock" includes:

- Equity securities registered or having unlisted trading privileges on a national securities exchange.
- Over the Counter (OTC) margin stock (appears on the list published by the Federal Reserve Board).
- OTC securities designated as qualified for trading in the national Market System under a designation plan approved by the SEC (NMS security).
- Debt securities convertible into margin stocks or carrying warrants or rights to subscribe to or purchase margin stocks.

JPMC 09753

CONFIDENTIAL

Texas Region Operating Procedures Manual — Compliance — Regulation U

- Securities issued by an investment company registered under Section 8 of the Investment Company Act with some limited exemptions.

The Purpose Statement must be completed in its entirety and be signed by the customer and a bank officer. The bank's standard practice on a revolving credit is to obtain the Purpose Statement at the time the credit arrangement is originally established rather than at the time of disbursement. A loan secured by mutual funds is considered secured by margin stock unless 95% of the assets of the fund are continuously invested in US government, agency, state or municipal obligations. When in doubt on a loan secured by stock, obtain a purpose statement on Form FR U-1.

Collateral Value Requirement — Purpose Credit Secured by Any Margin Stock

Regulation U specifies what loan value to give to collateral. Presently, margin stock has a maximum loan value of 50% of its current market value. Generally, puts, calls, and combinations thereof have no loan value for purposes of Regulation U.

All other collateral is valued at its good faith loan value which means that amount (not exceeding 100% of the current market value of the collateral) **which a bank, exercising sound banking judgment, would lend, without regard to the customer's other assets held as collateral in connection with unrelated transactions.** The "excess" margin required by Regulation U cannot be taken into account in determining the loan value of other collateral.

Single Credit Rule

The single credit rule treats a series of purpose loans, made at different times to the same customer, as a "single credit" for certain Regulation U purposes. If the bank lent purpose credit secured by margin stock it cannot 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.

If the bank extended unsecured purpose credit to a customer prior to the extension of purpose credit secured by margin stock, the credits are combined and treated as a single credit solely for the purposes of the withdrawal and substitution provisions of the regulation.

If the credit is purpose credit and the credit is not secured directly or indirectly by margin stock, then Regulation U collateral requirements do not apply unless the bank has previously extended purpose credit secured by margin stock. In that case, the bank cannot extend the unsecured purpose credit unless the combined credit does not exceed the maximum loan value of the collateral securing the prior credit.

Where purpose credit secured by any margin stock and non-purpose credit are extended to the same customer, the bank must treat the credits as two separate loans and may not rely upon the required collateral securing the purpose credit for the non-purpose credit.

Account Officer Responsibility

- Obtain an executed and completed Form FR U-1 for all stock-secured loans.
- Contact Commercial Loan Legal Services at (713) 750-2299 for further information or assistance.

Examples

Situation: Private Banker is making a loan to a customer to purchase EXXON stock and is securing the loan with Disney stock having a current market value of \$54,000. How much can the banker lend secured by this stock?

Answer: \$27,000.

Situation: Private Banker made an unsecured purpose credit to a customer for \$100,000. Customer has requested additional purpose credit for \$250,000 to be secured by margin stock. Can she make the loan if the margin stock's market value is \$520,000?

Answer: Yes. The stock has a maximum loan value of \$260,000 and therefore she may make the \$250,000 loan. Note,

Texas Region Operating Procedures Manual — Compliance — Regulation U

however, that in determining whether the customer can withdraw and substitute collateral she will have to aggregate the \$100,000 and \$250,000 loans and treat it as a single credit solely for the purposes of the withdrawal and substitution provisions.

Situation: Private Banker made a \$400,000 purpose credit secured by margin stock now valued at \$950,000 - can she make an unsecured purpose credit for \$80,000?

Answer: No. The prior purpose credit was secured, therefore the second purpose credit cannot be made unless the combined loan of \$480,000 does not exceed the maximum loan value of \$475,000.

Situation: Private banker is planning on making a mixed collateral loan of \$800,000 for the purpose of purchasing margin stock. She has margin stock with a current value of \$1,300,000 and a rent house appraised at \$170,000. Can she make the loan?

Answer: The question to ask, and the records to be made are as follows: The margin stock has a loan value equal to 50% of \$1,300,000 or \$650,000. Therefore, other collateral must secure \$150,000 (\$800,000-650,000).

The question then becomes: Would the private banker in good faith, while exercising sound banking judgment lend \$150,000 to this customer secured by the rent house without regard to the customer's other assets held as collateral (including the margin stock) in connection with unrelated transactions?

[Home](#) | [Department Profile](#) | [Organizational Chart](#) | [Policies & Procedures](#) | [Credit Bulletins](#) | [Feedback](#)

Modified: September 17, 2001 10:33 AM

CONFIDENTIAL

JPMC 09755