Regulatory Notice 21-24

Margin Interpretation Updates

FINRA Announces Updates to the Interpretations of FINRA's Margin Rule Regarding Minimum Equity

July 6, 2021

Notice Type
- Guidance

Suggested Routing
- Compliance
- Institutional
- Legal
- Margin
- Operations
- Risk
- Systems

Key Topics
- Initial Margin
- Margin
- Minimum Equity
- Withdrawals

Referenced Rules & Notices
- Rule 4210

Summary

This *Notice* announces, effective immediately, clarifications of interpretations of the FINRA margin rule regarding minimum equity requirements in FINRA Rule 4210(b).

Questions concerning this *Notice* should be directed to:

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Background & Discussion

FINRA Rule 4210 (Margin Requirements) specifies the margin requirements applicable to securities held in margin accounts, including both strategy-based margin accounts and portfolio margin accounts. FINRA maintains interpretations regarding FINRA Rule 4210, available on the Interpretations of FINRA's Margin Rule web page, where the interpretations immediately follow the section of the rule to which they relate. This *Notice* clarifies and updates the interpretations as discussed below.

Minimum Equity

FINRA Rule 4210(b) provides the amount of initial margin that must be in a customers' account.[1] Rule 4210(b) also limits when withdrawals of cash or securities may be made from the account.[2] Firms have raised questions regarding several aspects of this paragraph, including when the minimum equity amount is not required for fully paid securities and when excess cash in margin accounts that may hold fully paid securities may be withdrawn. FINRA is replacing Interpretation /02 to Rule 4210(b)[3] with modified interpretations divided into separate topics. Accordingly, new Interpretation /021 addresses the minimum equity requirements in a margin account[4]

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clarifying when the $2,000 amount is not required because securities may be fully paid. New Interpretation /021 also clarifies treatment of securities transactions resulting in positions covered by Rule 4210(e)(2)(F), (G) or (H) or other provisions of Rule 4210 that allow the member to take a capital charge in lieu of collecting margin. New Interpretation /022 incorporates the section of current Interpretation /02 that addresses the effect of market value decline on the minimum equity requirements. New Interpretation /023 clarifies when withdrawals are permissible. New Interpretation /024 clarifies minimum equity requirements for a cash account. Finally, new Interpretation /025 states the minimum equity requirements for a pattern day trader.

New Interpretation to FINRA Rule 4210(b)

/021 Minimum Equity

(a) Each new transaction in a customer margin account, including those instances where more than one margin account is permitted under Regulation T, is subject to the $2,000 minimum equity requirement of Rule 4210(b)(4) except that:

(1) Full cash payment for any security purchased will satisfy this requirement with respect to such purchase, even if the resulting equity is less than $2,000;

(2) Full cash payment for any option purchased will satisfy this requirement with respect to such purchase, even if the resulting equity is less than $2,000 (the purchase or sale of securities upon the exercise of an option, however, will constitute a new commitment for purposes of this requirement);

(3) The purchase of exempted securities;

(4) Securities transactions resulting in positions covered by Rule 4210(e)(2)(F),(G) or (H) or other provisions of Rule 4210 that allow the member to take a capital charge in lieu of collecting margin are not subject to this requirement;

(5) Even if the resulting equity is less than $2,000, the minimum equity requirement with respect to the sale of an option in the account would be satisfied by the deposit into the account or under an escrow agreement (as defined in Rule 4210(f)(2)(A)(xiv)) of:

(A) cash sufficient to satisfy the customer's payment obligation upon the assignment of the options if it is a put; or

(B) fully paid securities sufficient to satisfy the customer's delivery obligation upon the assignment of the option if it is a call;

(b) Except for transactions described in (a)(4) and (a)(5) above, every short sale is subject to the $2,000 minimum equity requirement regardless of the amount involved.

/022 Effect of Market Value Decline Below $2,000 Equity

If the equity in a margin account falls below $2,000 because of a decline in the market value of the security positions in the account and no new commitments are made, no deposit or liquidation is necessary. For the purpose of this Rule, a same-day substitution constitutes a new commitment.

/023 Withdrawals Below $2,000 Equity

No withdrawal may be made from a margin account that would leave less than $2,000 equity in the account after the withdrawal if the account has a debit balance, short position or other commitment. Withdrawals of cash or securities may be made from any account, even if after such withdrawal the equity in the account is less than $2,000, provided that:

(a) The account does not have a debit balance, short position or commitment after giving effect to the withdrawal;

(b) The withdrawal is in compliance with Regulation T and Rules 400 through 406 of SEC Customer Margin Requirements for Security Futures and Rules 41.42 through 41.49 under the CEA; and

(c) The account is not a pattern day trader (in which case the $25,000 minimum applies).

/024 Minimum Equity – Cash Account

The $2,000 minimum equity requirement of paragraph (b)(4) does not apply to transactions in a cash account, including transactions in when issued or when distributed securities in a cash account, even though Rule 4210(f)(3)(B) generally subjects cash account positions in such securities to the same maintenance margin requirements as in a margin account.

/025 Minimum Equity – Pattern Day Trader

Pattern day traders are subject to a $25,000 minimum equity requirement under Rule 4210(f)(8)(B)(iv)a.

Interpretation Updates

These interpretation updates are available on the Interpretations of FINRA's Margin Rule web page.

FINRA member firms and others that maintain the hardcopy version of the Interpretations of FINRA's Margin Rule may refer to the accompanying updated pages, containing the new interpretations, which are being made available to enable the replacement of existing pages in the hardcopy version of the Interpretations of FINRA's Margin Rule. The filing instructions for the new pages are as follows:

- Remove old pages 11-13 and insert new pages 11-14.

Endnotes

1. Rule 4210(b) requires a customer to deposit margin in cash or securities, which shall be at least the greater of: (1) the amount specified in Regulation T, or Rules 400 through 406 of SEC Customer Margin Requirements for Security Futures, or Rules 41.42 through 41.49 under the Commodity Exchange Act (CEA); (2) the amount specified in paragraph (c) of Rule 4210 (the maintenance margin requirements); (3) such greater amount as FINRA may from time to time require for specific securities; or (4) equity of at least $2,000 except that cash need not be deposited in excess of the cost of any security purchased (this equity and cost of purchase provision shall not apply to “when distributed” securities in a cash account). The minimum equity requirement for a “pattern day trader” is $25,000 pursuant to paragraph (f)(8)(B)(iv)a. of the rule.

2. Rule 4210(b) also provides that withdrawals of cash or securities may be made from any account which has a debit balance, “short” position or commitments, provided it is in compliance with Regulation T and SEA Rules 400 through 406 of the Customer Margin Requirements for Security Futures and Rules 41.42 through 41.49 under the CEA, and after such withdrawal the equity in the account is at least the greater of $2,000 ($25,000 in the case of a “pattern day trader”) or an amount sufficient to meet the maintenance margin requirements of the rule.

3. Current Interpretation /02 of Rule 4210(b) (which is replaced by the new Interpretations /021 through /025) provides:

   /02 Minimum Equity

   Every margin transaction must result in equity in the account of at least $2,000 except that payment in full for any security purchased will satisfy the requirement. Each customer account, including those instances where more than one margin account is permitted under Regulation T, is subject to the $2,000 requirement except for:

   - The purchase of “when distributed” securities in a cash account;
   - The purchase of exempt securities;
   - The purchase of an option ($2,000 needed upon exercise);
   - The sale of a put option where the exercise price is less than $20.00 per share;

   Every short sale, regardless of the amount involved, is subject to the $2,000 requirement. If the equity in an account falls below $2,000 because of a decline in the market value of the security(ies) and no new commitments are made, no deposit or liquidation is necessary. For the purpose of this Rule, a same-day substitution constitutes a new commitment. No withdrawal may be made from an account which would leave less than $2,000 equity in the account after the withdrawal.

4. FINRA notes that a good faith account (other than a non-securities account) is a margin account. After amendments to Regulation T created good faith accounts, the margin rule was amended to include good faith accounts within scope of the maintenance margin requirements of paragraph (c) but the changes in those amendments were not expressed throughout the rule. *See* Securities Exchange Act Release No. 42858 (May 30, 2000) 65 FR 36194, 36194 (June 7, 2000) (Order Approving NASD-99-05) (clarifying that “transactions in good faith accounts raise the same safety and soundness questions as transaction in cash and margin accounts.”) NASD, the predecessor to FINRA, amended NASD Rule 2520(c), which became FINRA Rule 4210(c), “to require all accounts, including good faith accounts, to maintain margin required by NASD Rule 2520.”