

INFORMATIONAL

Margin Requirements

SEC Approves Proposed Rule Change Relating To Margin For Exempted Borrowers, Good Faith Accounts, Joint Back Office Arrangements, Control And Restricted Securities, And Options Transactions; **Effective Date: August 21, 2000**

SUGGESTED ROUTING

The Suggested Routing function is meant to aid the reader of this document. Each NASD member firm should consider the appropriate distribution in the context of its own organizational structure.

- Executive Representatives
- Institutional
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KEY TOPICS

- Margin
- NASD Rule 2520
- Options

Executive Summary

On May 30, 2000, the Securities and Exchange Commission (SEC) approved amendments to National Association of Securities Dealers, Inc. (NASD[®]) Rule 2520 relating to margin requirements for exempted borrowers, good faith accounts, joint back office (JBO) arrangements, control and restricted securities, and options transactions.¹ The amendments become effective on August 21, 2000. There is a six-month phase-in period for the implementation of the amendments relating to JBO arrangements.

Questions concerning this *Notice* may be directed to Susan DeMando, Director, Financial Operations, Member Regulation, NASD Regulation, Inc. (NASD RegulationSM) at (202) 728-8411; or Stephanie M. Dumont, Assistant General Counsel, Office of General Counsel, NASD Regulation, at (202) 728-8176.

Attachment A includes the text of the amendments to Rule 2520.

Highlights Of Rule Changes

The significant changes to Rule 2520 are discussed below.

Exempted Borrowers And Good Faith Accounts

Under recent changes to Regulation T, the Federal Reserve Board has created a new account category called the "good faith account" to replace the "non-purpose," "arbitrage," and "government securities" accounts.² In the good faith account, a customer may purchase certain securities (exempted securities, non-equity securities, money market mutual funds, and exempted securities mutual funds)

on "good faith" margin (the amount of margin specified by the creditor in the exercise of sound credit judgment) or the margin specified by the applicable regulatory authority, whichever is greater. Regulation T no longer specifies initial margin, payment, and liquidation time frames for transactions in these securities in a good faith account.

NASD Regulation believes that transactions in good faith accounts can raise the same financial concerns as transactions in cash and margin accounts. Accordingly, the amendments to Rule 2520(c) require all accounts, including good faith accounts, to maintain margin as required by NASD Rule 2520. Cash accounts will continue to be subject only to certain specific requirements applicable to cash accounts, not to the overall requirements of the rule.

In addition, the Federal Reserve Board established a classification of exempted borrowers that are exempt from Regulation T. An "exempted borrower," as defined in Regulation T, is a broker/dealer of which "a substantial portion of whose business consists of transactions with persons other than brokers or dealers."³ The amendments codify this exemption from Regulation T by excluding "exempted borrowers," as defined in Regulation T, from the definition of "customer" in NASD Rule 2520(a)(3), except for the proprietary account of a broker/dealer carried by a member pursuant to NASD Rule 2520(e)(6). Thus, proprietary accounts of an introducing member that are carried or cleared by another member will remain subject to the equity requirements of NASD Rule 2520(e)(6).

Joint Back Office Arrangements

Section 220.7(c) of Regulation T allows special margin treatment for broker/dealers without clearing operations, known as "JBO participants," that invest in a "clearing and servicing" broker/dealer, known as a "JBO broker." The amendments provide certain regulatory requirements for initiating and maintaining JBO arrangements established pursuant to Section 220.7 of Regulation T, as follows. These amendments should be phased in over the next six months and must be implemented by February 26, 2001.

A JBO broker must be a clearing or carrying firm in accordance with the requirements of Regulation T. Under the amendments, a JBO broker is required to:

- Notify the NASD in writing⁴ prior to establishing a JBO arrangement.
 - Maintain a minimum tentative net capital⁵ of \$25 million, unless the JBO broker's primary business consists of the clearance of options market-maker accounts,⁶ then it may elect to maintain a minimum net capital⁷ of \$7 million, provided it also includes gross deductions for JBO participant accounts in its ratio of gross options market-maker deductions to net capital pursuant to SEC Rule 15c3-1 (Net Capital Rule).
 - Notify the NASD promptly in writing⁸ if tentative net capital or net capital falls below the requirements outlined above and take action to correct such deficiency within three business days or, if it fails to do so, the JBO broker is prohibited from accepting new transactions pursuant to the JBO arrangement.
- Deduct from its net capital, haircut requirements pursuant to the Net Capital Rule that are in excess of the equity maintained in the accounts of the JBO participants.
 - Maintain a written risk analysis methodology for assessing the amount of credit extended to JBO participants. Minimum guidelines for acceptable risk procedures should include the following:
 - ◆ Procedures for obtaining and reviewing appropriate account documentation and financial information;
 - ◆ Procedures and guidelines for the determination, review, and approval of credit limits;
 - ◆ Procedures and guidelines for monitoring credit risk exposure to the organization relating to JBO participants;
 - ◆ Procedures and guidelines for the use of stress testing of accounts in order to monitor market risk exposure; and
 - ◆ Procedures providing for the regular review and testing of these risk management procedures by an independent unit such as internal audit, risk management, or other comparable group.

A JBO participant must be a registered broker/dealer subject to the Net Capital Rule. The JBO participant is required to:

- Maintain an ownership interest in the JBO broker pursuant to Regulation T of the Federal Reserve Board; and
- Maintain a minimum net liquidating equity of \$1 million in the JBO account, exclusive of the

JBO participant's ownership interest in the JBO broker.

If the JBO participant's liquidating equity falls below \$1 million, the equity deficiency must be met within five business days in order to ensure continued eligibility as a JBO participant. A JBO participant that loses its JBO participant status generally would become subject to customer margin account requirements pursuant to Regulation T, if applicable, and margin requirements pursuant to other provisions of Rule 2520.

Control And Restricted Securities

Rule 2520(e)(8)(C)(ii) has been modified to address an anomaly currently within the "Concentration Reduction" provision, which imposes a higher requirement on accounts that have deposited more control and restricted securities than are required to collateralize the extension of credit. To eliminate this unintended penalty, the amount of "excess securities," as defined in the amended Rule 2520, will be excluded from the Concentration Reduction calculation.⁹ Thus, the Concentration Reduction calculation will be performed on an aggregate position that is only as large as the collateral necessary to support a margin loan of 50 percent.

In addition, the amendments expand the exception in paragraph (e)(8) to include all restricted securities that are then saleable, including affiliate securities, pursuant to Rules 144(k), 145(d)(2), or 145(d)(3) of the Securities Act of 1933. Accordingly, those customer-owned, restricted securities that are then saleable and can be sold under SEC Rule 144(k) would be subject to the same maintenance margin requirements that currently apply to ordinary stock (25 percent).

Broker/Dealer Margin Requirements

Subparagraphs (e)(5) and (e)(6) of Rule 2520 currently require a carrying broker/dealer to deduct from its net capital the difference between the equity maintained in the account of a specialist, market maker, or broker/dealer and the required maintenance margin under NASD Rule 2520. The amendments to subparagraphs (e)(5) and (e)(6) require the carrying broker/dealer to deduct from its net capital the difference between the equity maintained in the account of a specialist, market maker, or broker/dealer and the required haircut in accordance with the Net Capital Rule. For example, in the case of a long position in an equity security, the amendments require a carrying broker to compute its net capital deduction for deficient specialist, market maker, and broker/dealer accounts based on the 15 percent haircut requirement of paragraph (c)(2)(vi)(J) of the Net Capital Rule, rather than the 25 percent maintenance margin requirement of NASD Rule 2520(c)(1).

Options Transactions

Rule 2520(f)(2)(L) incorporates provisions currently contained in Regulation T regarding "exclusive designation." This provision will allow a customer to designate which security position in an account to use to cover the requested margin at the time the option order is entered, provided the member offers such a service. NASD Rule 2520(f)(2)(M)(i) permits options transactions in customer cash accounts if the transaction is permissible under Section 220.8 of Regulation T.

Effective Date Of Amendments

These amendments become effective on August 21, 2000. However, there is a six-month phase-in period for the amendments relating to JBO arrangements, which must be implemented by February 26, 2001.

Endnotes

¹See Securities Exchange Act Release No. 42858 (May 30, 2000), 65 Fed. Reg. 36194 (June 7, 2000) (File No. SR-NASD-99-05).

²See Board of Governors of the Federal Reserve System Docket Nos. R-0905, R-0923, and R-0944, 63 Fed. Reg. 2806 (January 16, 1998).

³12 CFR 220.2.

⁴Notification should be made to the appropriate NASD District Office and to the Financial Operations Department, NASD Regulation, 1735 K Street, NW, Washington, DC 20006.

⁵The term "tentative net capital" generally refers to net capital before haircuts and undue concentration charges on proprietary securities and options positions. Haircuts are specified percentages of the market value of a broker/dealer's proprietary securities by which a broker/dealer must reduce its net worth under Rule 15c3-1 under the Securities Exchange Act of 1934 (the "Net Capital Rule" or "SEC Rule 15c3-1").

⁶The clearance of options market-maker accounts will be deemed a broker/dealer's primary business if a minimum of 60 percent of the aggregate deductions in the broker/dealer's ratio of gross options market-maker deductions to net capital (including gross deductions for JBO participant accounts) are options market-maker

deductions. Subparagraph (c)(2)(x) of the Net Capital Rule limits the amount of specialist and market-maker options positions a firm may guarantee, endorse, or carry to a ratio of 10 to 1 of options market maker and specialist deductions to net capital. In addition, subparagraph (a)(6) of the Net Capital Rule exempts an option market maker and specialist from the haircut provisions of the Net Capital Rule provided that, among other things, the firm maintains liquidating equity in its account equal to the percentage described in subparagraph (a)(6)(iii)(A) of the Net Capital Rule.

⁷The term "net capital" is defined under the Net Capital Rule and is generally calculated by deducting illiquid assets from a firm's "net worth," as determined under Generally Accepted Accounting Principles (GAAP), adding to that amount properly subordinated debt under Appendix D of the Net Capital Rule, and further deducting haircuts from securities held in the firm's proprietary accounts.

⁸Notification should be made to the appropriate NASD District Office and to the Financial Operations Department, NASD Regulation, 1735 K Street, NW, Washington, DC 20006.

⁹The term "excess securities" is defined as the amount of securities, if any, by which the aggregate position in control and restricted securities of any one issue exceeds the aggregate amount of securities that would be required to support the aggregate credit extended on such control and restricted securities if the applicable margin requirement were 50 percent.

ATTACHMENT A

Text Of Amendments

(Note: New language is underlined; deletions are in brackets.)

2520. Margin Requirements

(a) Definitions

For purposes of this paragraph, the following terms shall have the meanings specified below:

(1) – (2) No Change

(3) The term “customer” means any person for whom securities are purchased or sold or to whom securities are purchased or sold whether on a regular way, when issued, delayed or future delivery basis. It will also include any person for whom securities are held or carried and to or for whom a member extends, arranges or maintains any credit. The term will not include the following: (A) a broker or dealer from whom a security has been purchased or to whom a security has been sold for the account of the member or its customers[.], or (B) an “exempted borrower” as defined by Regulation T of the Board of Governors of the Federal Reserve System (“Regulation T”), except for the proprietary account of a broker/dealer carried by a member pursuant to paragraph (e)(6) of this Rule.

(4) – (8) No Change

(b) Initial Margin

For the purpose of effecting new securities transactions and commitments, the customer shall be required to deposit margin in cash and/or securities in the

account which shall be at least the greater of:

(1) the amount specified in Regulation T [of the Board of Governors of the Federal Reserve System]; or

(2) the amount specified in paragraph (c)(3) of this Rule; or

(3) such greater amount as the Association 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).

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 [of the Board of Governors of the Federal Reserve System] and after such withdrawal the equity in the account is at least the greater of \$2,000 or an amount sufficient to meet the maintenance margin requirements of this paragraph.

(c) Maintenance Margin

The margin which must be maintained in all [margin] accounts of customers, except for cash accounts subject to other provisions of this rule, shall be as follows:

(1) 25 percent of the current market value of all securities “long” in the account; plus

(2) \$2.50 per share or 100 percent of the current market value, whichever amount is greater, of each stock “short” in

the account selling at less than \$5.00 per share; plus

(3) \$5.00 per share or 30 percent of the current market value, whichever amount is greater, of each stock “short” in the account selling at \$5.00 per share or above; plus

(4) 5 percent of the principal amount or 30 percent of the current market value, whichever amount is greater, of each bond “short” in the account; plus

(5) In the case of securities listed on the Emerging Company Marketplace of the American Stock Exchange (AMEX), 100 percent of the market value in cash, of each security held “long” in the account, unless the AMEX determines that the security satisfies the criteria enumerated in Sections 220.17(a) and (b) of Regulation T of the Board of Governors of the Federal Reserve System for inclusion and continued inclusion on the List of OTC Margin Stocks, except for the requirement relating to the number of dealers in Sections 220.17(a)(1) and (b)(1)].

(d) No Change

(e) Exceptions to Rule

The foregoing requirements of this [paragraph] Rule are subject to the following exceptions:

(1) No Change

(2) Exempted Securities, Marginable Corporate Debt Securities and Baskets

(A) – (B) No Change

(C) Non-Convertible Corporate Debt Securities

On any positions in non-convertible corporate debt securities, which are listed or traded on a registered national securities exchange or qualify as an "OTC margin bond," as defined in Section 220.2(t) of Regulation T [of the Board of Governors of the Federal Reserve System], the margin to be maintained shall be 20 percent of the current market value or 7 percent of the principal amount, whichever amount is greater, except on mortgage related securities as defined in Section 3(a)(41) of the Act the margin to be maintained for an exempt account shall be 5 percent of the current market value. For purposes of this subparagraph, an exempt account shall be defined as a member, non-member broker/dealer, "designated account" or any person having net tangible assets of at least sixteen million dollars.

(D) – (F) No Change

(3) Joint Accounts in Which the Carrying Member or a Partner or Stockholder Therein Has an Interest

In the case of a joint account carried by a member in which such member, or any partner, or stockholder (other than a holder of freely transferable stock only) of such member participates with others, each participant other than the carrying member shall maintain an equity with respect to such interest pursuant to the margin provisions of this paragraph as if such interest were in a separate account.

Pursuant to the Rule 9600 Series, the Association may grant an exemption from the

provisions of paragraph (e)(3), if the account is[:]

[(A)] confined exclusively to transactions and positions in exempted securities[;

(B) maintained as a Market Functions Account conforming to the conditions of Section 220.12(e) (Odd-lot dealers) of Regulation T of the Board of Governors of the Federal Reserve System; or

(C) maintained as a Market Functions Account conforming to the conditions of Section 220.12(c) (Underwritings and Distributions) of Regulation T of the Board of Governors of the Federal Reserve System and each other participant margins his share of such account on such basis as the Association may prescribe].

(4) No Change

(5) Specialists' and Market Makers' Accounts

(A) A member may carry the account of an "approved specialist or market maker," which account is limited to specialist or market making transactions, upon a margin basis which is satisfactory to both parties. The amount of any deficiency between the equity in the account and the [margin required by the other provisions of this paragraph and the] haircut requirements pursuant to SEC Rule 15c3-1 shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

For the purpose of this subparagraph, the term "approved specialist or market maker" means either:

(i) a specialist or market maker, who is deemed a specialist for all purposes under the Act and who is registered pursuant to the rules of a national securities exchange; or

(ii) an OTC market maker or third market maker, who meets the requirements of Section 220.7(g)(5)[12(d)] of Regulation T [of the Board of Governors of the Federal Reserve System].

(B) In the case of a joint account carried by a member in accordance with subparagraph (i) above in which the member participates, the equity maintained in the account by the other participants may be in any amount which is mutually satisfactory. The amount of any deficiency between the equity maintained in the account by the other participants and their proportionate share of the [margin required by the other provisions of this paragraph] the haircut requirements pursuant to SEC Rule 15c3-1 shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

(6) Broker/Dealer Accounts

(A) A member may carry the proprietary account of another broker/dealer, which is registered with the Commission, upon a margin basis which is satisfactory to both parties, provided the requirements of Regulation T [of the Board of Governors of the Federal Reserve System] are adhered to and the account is not carried in a deficit equity condition. The amount of any deficiency between the equity

maintained in the account and the [margin required by the other provisions of this paragraph] haircut requirements pursuant to SEC Rule 15c3-1 shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

(B) Joint Back Office Arrangements

An arrangement may be established between two or more registered broker/dealers pursuant to Regulation T Section 220.7, to form a joint back office ("JBO") arrangement for carrying and clearing or carrying accounts of participating broker/dealers. Members must provide written notification to the Association prior to establishing a JBO arrangement.

(i) A carrying and clearing, or carrying member must:

a. maintain a minimum tentative net capital of \$25 million as computed pursuant to SEC Rule 15c3-1, except that a member whose primary business consists of the clearance of options market-maker accounts may carry JBO accounts provided that it maintains a minimum net capital of \$7 million as computed pursuant to SEC Rule 15c3-1. In addition, the member must include in its ratio of gross options market maker haircuts required by the provisions of SEC Rule 15c3-1 gross deductions for JBO participant accounts. Clearance of option market maker accounts shall be deemed a broker/dealer's primary business if a

minimum of 60% of the aggregate deductions in the above ratio are options market maker deductions. In the event that a carrying and clearing, or a carrying member's tentative net capital, or net capital, respectively, has fallen below the above requirements, the firm shall:
1. promptly notify the Association in writing of such deficiency, 2. take appropriate action to resolve such deficiency within three consecutive business days, or not permit any new transactions to be entered into pursuant to the JBO arrangement;

b. maintain a written risk analysis methodology for assessing the amount of credit extended to participating broker/dealers which shall be made available to the Association on request; and

c. deduct from net capital haircut requirements pursuant to SEC Rule 15c3-1 amounts in excess of the equity maintained in the accounts of participating broker/dealers.

(ii) A participating broker/dealer must:

a. be a registered broker/dealer subject to the SEC's net capital requirements;

b. maintain an ownership interest in the carrying/clearing member organization pursuant to Regulation T of the Federal Reserve Board, Section 220.7; and

c. maintain a minimum liquidating equity of \$1 million in the JBO arrangement exclusive of the ownership interest established in (ii)b. above. When the minimum liquidating equity decreases below the \$1 million requirement, the participant must deposit an amount sufficient to eliminate this deficiency within 5 business days or be subject to margin account requirements prescribed for customers in Regulation T, and the margin requirements pursuant to the other provisions of this Rule.

(7) Nonpurpose Credit

In a nonsecurities credit account, a member may extend and maintain nonpurpose credit to or for any customer without collateral or on any collateral whatever, provided,

(A) the account is recorded separately and confined to the transactions and relations specifically authorized by Regulation T [of the Board of Governors of the Federal Reserve System];

(B) the account is not used in any way for the purpose of evading or circumventing any regulation of the Association or of the Board of Governors of the Federal Reserve System; and

(C) the amount of any deficiency between the equity in the account and the margin required by the other provisions of this paragraph shall be charged against the member's net capital as provided in SEC Rule 15c3-1.

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The term “nonpurpose credit” means an extension of credit other than “purpose credit” as defined in Section 220.2[(u)] of Regulation T [of the Board of Governors of the Federal Reserve System].

(8) Shelf-Registered, Control and Restricted Securities

(A) No Change

(B) Control and Restricted Securities—The equity in accounts of customers for control securities and other restricted securities of issuers who continue to maintain a consistent history of filing annual and periodic reports in timely fashion pursuant to the formal continuous disclosure system under the Act, which are subject to Rule 144 or 145(d) under the Securities Act of 1933, shall be 40 percent of the current market value of such securities “long” in the account, provided the member:

(i) in computing net capital, deducts any margin deficiencies in customers’ accounts based upon a margin requirement as specified in subparagraph (C)(ii) [(iii)] below for such securities and values only that amount of such securities which are then salable under Rule 144 or 145(d) under the Securities Act of 1933 in conformity with all of the applicable terms and conditions thereof, for purposes of determining such deficiencies; and

(ii) No Change

(C) Additional Requirements on Shelf-Registered Securities and Control and Restricted

Securities - A member extending credit on shelf-registered, control and other restricted securities in margin accounts of customers shall be subject to the following additional requirements:

(i) The Association may at any time require reports from members showing relevant information as to the amount of credit extended on shelf-registered, control and restricted securities and the amount, if any, deducted from net capital due to such security positions.

(ii) Concentration Reduction. A concentration exists whenever the aggregate position in control and restricted securities of any one issue, excluding excess securities (as defined below), exceeds:

a. 10 percent of the outstanding shares or

b. 100 percent of the average weekly volume during the preceding three-month period. Where a concentration exists, for purposes of computing subparagraph (B)(i) above, the margin requirement on such securities shall be, based on the greater of (ii)a. or b. above, as specified below:

***No Change to Table ***

For purposes of this subparagraph (e)(8)(C)(ii), “excess securities” shall mean the amount of securities, if any, by which the aggregate position in control and restricted securities of any one issue

exceeds the aggregate amount of securities that would be required to support the aggregate credit extended on such control and restricted securities if the applicable margin requirement were 50%.

(D) Restricted Securities - Securities either:

(i) [held by non-affiliates of the issuer which are] then salable [by the non-affiliate] pursuant to the terms and conditions of Rule 144(k) under the Securities Act of 1933, or

(ii) [which have been acquired by non-affiliates of the issuer in connection with a Rule 145(a) transaction under the Securities Act of 1933 which are] then salable [by such non-affiliate] pursuant to the terms and conditions of Rule 145(d)(2) or (d)(3) under such Act,

shall not be subject to the provisions of this subparagraph [(H)] (e)(8), provided that the issuer continues to maintain a consistent history of filing annual and periodic reports in timely fashion pursuant to the formal continuous disclosure system under the Act.

(f) Other Provisions

(1) – (2)(H)(iii) No Change

(2)(H)(iv) Where a put or call is carried “short” in the account of a customer against a letter of guarantee in form satisfactory to the Association and issued by a third party custodian bank or trust company (the guarantor), which letter of guarantee is held in the account at the time the put or call is written, or is received in the

account promptly thereafter, no margin need be required on the put or call.

In the case of a call on a broad index stock group, the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter either cash, cash equivalents, one or more qualified securities, or any combination thereof, having an aggregate market value, computed as at the close of business on the day the call is written, of not less than 100 percent of the aggregate current index value computed as at the same time and that the guarantor will promptly pay the member the exercise settlement amount in the event the account is assigned an exercise notice. The letter of guarantee may provide for substitution of qualified securities held as collateral provided that the substitution shall not cause the value of the qualified securities held to be diminished. A qualified security means an equity security, other than a warrant, right or option, that is traded on any national securities exchange; or any equity security, other than a warrant, listed in the current list of Over-the-Counter Margin Stocks as published by the Board of Governors of the Federal Reserve System.

In the case of a call on any other option contract, the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter, the underlying security (or a security immediately convertible into the underlying security without the payment of money) or foreign currency and that the guarantor will promptly deliver to the member the underlying security or foreign

currency in the event the account is assigned an exercise notice.

In the case of a put on an option contract (including a put on a broad index stock group), the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter, cash or cash equivalents which have an aggregate market value, computed as at the close of business on the day the put is written, of not less than 100 percent of the aggregate exercise price of the put and that the guarantor will promptly pay the member the exercise settlement amount (in the case of a put on a broad index stock group) or the aggregate exercise price (in the case of any other put on an option contract) in the event the account is assigned an exercise notice. Cash equivalents shall mean those instruments referred to in Section 220.2 of Regulation T [of the Board of Governors of the Federal Reserve System].

(f)(2)(l) – (K) No Change

(L) Exclusive designation - A customer may designate at the time an option order is entered which security position held in the account is to serve in lieu of the required margin, if such service is offered by the member; or the customer may have a standing agreement with the member as to the method to be used for determining on any given day which security position will be used in lieu of the margin to support an option transaction. Any security held in the account which serves in lieu of the required margin for a short put or short call shall be unavailable to support any

other option transaction in the account.

(M) Cash account transactions - A member may make option transactions in a customer's cash account, provided that the transaction is permissible under Regulation T, Section 220.8.

(3) "When Issued" and "When Distributed" Securities

(A) Margin Accounts

The margin to be maintained on any transaction or net position in each "when issued" security shall be the same as if such security were issued.

Each position in a "when issued" security shall be margined separately and any unrealized profit shall be of value only in providing the amount of margin required on that particular position.

When an account has a "short" position in a "when issued" security and there are held in the account securities upon which the "when issued" security may be issued, such "short" position shall be marked to the market and the balance in the account shall for the purpose of this [paragraph (c)] Rule be adjusted for any unrealized loss in such "short" position.

(B) Cash Accounts

On any transaction or net position resulting from contracts for a "when issued" security in an account other than that of a member, non-member broker/dealer, or a "designated account," equity must be maintained equal to the margin required were such transaction

or position in a margin account.

On any net position resulting from contracts for a "when issued" security made for or with a non-member broker/dealer, no margin need be required, but such net position must be marked to the market.

On any net position resulting from contracts for a "when issued" security made for a member or for or with a "designated account," no margin need be required and such net position need not be marked to the market. However, where such net position is not marked to the market, an amount equal to the loss at the market in such position shall be charged against the member's net capital as provided in SEC Rule 15c3-1.

The provisions of this subparagraph [(B)](f)(3) shall not apply to any position resulting from contracts on a "when issued" basis in a security:

(i) which is the subject of a primary distribution in connection with a bona fide offering by the issuer to the general public for "cash," or

(ii) which is exempt by the Association as involving a primary distribution.

The term "when issued" as used herein also means "when distributed."

(f)(4) – (5) No Change

(f)(6) Time Within Which Margin or "Mark to Market" Must Be Obtained

The amount of margin or "mark to market" required by any provision of this [paragraph (c)] Rule shall be obtained as promptly as possible and in any event within fifteen business days from the date such deficiency occurred, unless the Association has specifically granted the member additional time.

(f)(7) Practice of Meeting Regulation T Margin Calls by Liquidation Prohibited

When a "margin call," as defined in Section 220.2[(1)] of Regulation T [of the Board of Governors of the Federal Reserve System], is required in a customer's account, no member shall permit a customer to make a practice of either deferring the deposit of cash or securities beyond the time when such transactions would ordinarily be settled or cleared, or meeting the margin required by the liquidation of the same or other commitments in the account.

This prohibition on liquidations shall only apply to those accounts that, at the time of liquidation, are not in compliance with the equity to be maintained pursuant to the provisions of this Rule.

(f)(8)(A) No Change

(f)(8)(B) Day-Trading

The term "day-trading" means the purchasing and selling of the same security on the same day. A "day-trader" is any customer whose trading shows a pattern of day-trading.

Whenever day-trading occurs in a customer's margin account the margin to be maintained

shall be the margin on the "long" or "short" transaction, whichever occurred first, as required pursuant to the other provisions of this Rule. When day-trading occurs in the account of a "day-trader" the margin to be maintained shall be the margin on the "long" or "short" transaction, whichever occurred first, as required by Regulation T [of the Board of Governors of the Federal Reserve System] or as required pursuant to the other provisions of this Rule, whichever amount is greater.

When the equity in a customer's account, after giving consideration to the other provisions of this Rule, is not sufficient to meet the requirements of subparagraph (i) or (ii) hereof, additional cash or securities must be received into the account to meet any deficiency within seven business days of the trade date.

(9) Free-Riding in Cash Accounts Prohibited

No member shall permit a customer (other than a broker/dealer or a "designated account") to make a practice, directly or indirectly, of effecting transactions in a cash account where the cost of securities purchased is met by the sale of the same securities. No member shall permit a customer to make a practice of selling securities with them in a cash account which are to be received against payment from another broker/dealer where such securities were purchased and are not yet paid for. A member transferring an account which is subject to a Regulation T 90-day freeze to another member firm

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shall inform the receiving member of such 90-day freeze.

The provisions of Section 220.8(c) of Regulation T [of the Board of Governors of the Federal Reserve System] dictate

the prohibitions and exceptions against customers' free-riding. Members may apply to the Association in writing for waiver of a 90-day freeze not exempted by Regulation T.

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