

# Notice to Members

JULY 2005

## SUGGESTED ROUTING

Legal and Compliance  
Operations  
Senior Management

## KEY TOPICS

Exchange Act Rule 15c3-1  
Exchange Act Rule 15c3-3  
Federal Reserve Board Regulation T  
NASD Rule 2520  
Systems  
Unexpected Close

## GUIDANCE

### Unexpected Close of Securities Markets

#### Executive Summary

This *Notice* provides guidelines to members regarding the applicability of Exchange Act Rules 15c3-1 and 15c3-3, NASD Rule 2520, and Federal Reserve Board Regulation T in the event the securities markets unexpectedly close. The *Notice* explains the circumstances under which the day of the unexpected close is to be considered a “regular business day” and the circumstances under which it should be considered a “non-business day.”

#### Questions/Further Information

Questions regarding this *Notice* may be directed to Susan M. DeMando, Associate Vice President, Financial Operations, Department of Member Regulation, at (202) 728-8411.

#### Background and Discussion

On occasion, the securities markets may unexpectedly close for business; e.g., on a national day of mourning. However, the Federal Reserve regional banks, other banks, and the Depository Trust & Clearing Corporation (DTCC) may elect to remain open for clearance and settlement of securities. Such an event occurred on June 11, 2004, the day of former President Ronald Reagan’s funeral.

In anticipation of future unexpected closings similar to the closing that occurred on June 11, 2004, this *Notice* provides members with guidelines regarding the applicability of various regulations.<sup>1</sup> NASD members should follow these guidelines in the event of an unexpected close. This *Notice* will hereafter refer to an unexpected close of securities markets as “that day.”

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1. Regarding the applicable regulatory requirements pursuant to Exchange Act Rules 15c3-1 and 15c3-3, NASD Rule 2520, and Federal Reserve Board Regulation T, if the banks and DTCC are open, members should consider “that day” as a regular business day for the following:

**(A) Exchange Act Rule 15c3-1 (Net Capital)**

For aging purposes, in determining net capital charges (fail to deliver, suspense charges, etc.), “that day” should be considered as a regular business day.

**(B) Exchange Act Rule 15c3-3 (Reserve Formula and Possession or Control)**

- (1) If “that day” occurs on a Friday, the weekly reserve formula computation should be prepared, as usual, as of close of business on Friday, with the deposit requirement (if any) to be made by 10 a.m. on the second business day following the computation date.
- (2) If “that day” occurs on the normal month-end date, the reserve formula computation should be prepared, as usual, as of close of business on the month-end date with the deposit requirement (if any) to be made by 10 a.m. on the second business day following the computation date.
- (3) For purposes of possession or control requirements, bank loan and stock loan recalls, if required, should be effected on “that day.”

**(C) Federal Reserve Board Regulation T (Extensions)**

Margin extensions due on “that day” can be filed either on “that day” or on the next business day (as of “that day”). All subsequent extensions required to be filed after “that day” should be filed on the normal due date, counting “that day” as a business day. However, if the request for an extension has expired or is denied, “that day” should be treated as a non-business day since securities cannot be liquidated when the primary market where the securities are traded is closed.

**(D) NASD Rule 2520 (Margin Calls)**

For maintenance margin calls, pursuant to NASD Rule 2520(f)(6), “that day” should be counted as a regular business day.

**(E) Federal Reserve Board Regulation T (DKs on COD Deliveries)**

Extensions on DK’d COD transactions due on “that day” can be filed either on “that day” or on the next business day (as of “that day”). If “that day” falls within the granted two-day extension period, members may treat “that day” as either a business day or a non-business day. All subsequent extensions should be filed on the normal due date, counting “that day” as a business day. However, if the request for an extension has expired or is denied, “that day” should be treated as a non-business day since securities cannot be liquidated when the primary market where the securities are traded is closed.

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**(F) Exchange Act Rule 15c3-3(m) (Sell Order Extensions)**

Extensions on customers' sell orders under Exchange Act Rule 15c3-3(m) due on "that day" can be filed either on "that day" or on the next business day (as of "that day"). All subsequent extensions should be filed on the normal due date, counting "that day" as a business day. However, if the request for an extension has expired or is denied, "that day" should be treated as a non-business day since securities cannot be purchased when the primary market where the securities are traded is closed.

**(G) NASD Rule 2520(f)(8)(B)(iv)(e) (Day Trading Requirements)**

Funds deposited into a day trader's account to meet the minimum equity or maintenance margin requirements of NASD Rule 2520(f)(8)(B) cannot be withdrawn for a minimum of two business days following the close of business on the day of deposit. In making this determination, "that day" should be counted as a business day.

2. For regulatory purposes, in regards to the applicable requirements pursuant to Exchange Act Rules 17a-5(a) and (b), members should consider the day the securities markets are closed ("that day") as a non-business day for the following:

**(A) Exchange Act Rule 17a-5(a) (FOCUS Report)**

For purposes of determining the FOCUS Report due date, "that day" should not be considered as a business day.

**(B) Exchange Act Rule 17a-5(b)**

For filing a report upon termination of membership interest, "that day" should not be considered as a business day.

3. For purposes of Exchange Act Rule 15c3-3 (Reserve Formula Computation), if "that day" occurs on a Friday or on a month-end date and money markets funds are closed, the SEC has granted two options to members when computing its reserve formula:

**(A) Recording of Bookkeeping Entries on Liquidation/Sweep of Money Market Funds:**

Members can decide to record the bookkeeping entries on the liquidation of customers' money market funds or on the sweep of customers' balances into money market funds that are not open on "that day." Members can net the receivable and the payable only between the same family of funds. If this netting results in a net receivable from the fund, nothing further needs to be done. In addition, any unsecured receivables due from the money market fund may be considered as an allowable asset for net capital purposes for "that day" only if the following conditions are met:

- (1) the broker-dealer has control over the money market fund; and
- (2) the customer of the broker-dealer cannot access the fund; and
- (3) the broker-dealer must receive the money from the fund on the next business day.

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However, if recording the bookkeeping entries results in a net payable to the fund, that amount needs to be locked up on “that day” into the broker-dealer’s 15c3-3 Reserve Bank Account. A separate 15c3-3 Reserve Bank Account need not be set up for this deposit. The required deposit can be made into the broker-dealer’s already established 15c3-3 Reserve Bank Account. The funds can then be withdrawn on the next business day, directly from the 15c3-3 Reserve Bank Account, to pay the money market fund. The amount of funds deposited and the subsequent withdrawal for payment of such funds must be separately identified on the broker-dealer’s records. In this option, the reserve formula computation as of close of business of “that day” would not include the customers’ free credit balances, nor would it include any customer debits related to trades that settled on “that day” who had money market positions.

Whether the reserve formula computation of “that day” results in an excess of total debits over total credits or in an excess of total credits over total debits has no impact on the requirement that any net payable to a money market fund must be locked up into a 15c3-3 Reserve Bank Account on “that day.”

**(B) Non-Recording of Bookkeeping Entries on Liquidation/Sweep of Money Market Funds:**

Members can decide not to record the bookkeeping entries on the liquidation of customers’ money market funds or on the sweep of customers’ balances into money market funds that are not open on “that day.” Therefore, the reserve formula computation as of the close of business “that day” would include customers’ free credit balances that were not swept, as well as customer debits relating to their trades that settled on “that day,” even though the customers had money market positions. Members can, if needed, use the securities of the customers who had debit balances in their customer accounts to finance their business.

4. For securities lending, it is understood that the business will continue to operate as usual on “that day,” even though the primary securities markets will be closed.
5. On a case-by-case basis, NASD will consider a request for relief from regulatory requirements resulting from the closing of the securities markets on “that day.” In cases where undue hardship can be demonstrated, members should contact Susan M. DeMando, Associate Vice President, Financial Operations, Department of Member Regulation, at (202) 728-8411 to discuss the specific relief sought and the reason for such relief.

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## Endnote

- 1 The guidelines in this *Notice* are consistent with those provided by the New York Stock Exchange (NYSE) in NYSE Information Memo, Number 05-25, April 8, 2005.

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