

January 19, 1998

Katherine A. England
Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549
Mail Stop 10-1

Re: **File No. SR-NASD-99-05** - Amendments to Rule 2520 (Margin Rules)
Relating to Margin for Exempted Borrowers, Good Faith Accounts, Joint Back Office
Arrangements and Options Transactions

Dear Ms. England:

Pursuant to Rule 19b-4, enclosed herewith is the above-numbered rule filing. Also enclosed is a 3-1/2" disk containing the rule filing in Microsoft Word 7.0 to facilitate production of the Federal Register release.

If you have any questions, please contact Elliott R. Curzon, Office of General Counsel, NASD Regulation, Inc., at (202) 728-8451; e-mail curzone@nasd.com. The fax number of the Office of General Counsel is (202) 728-8264.

Very truly yours,

Alden S. Adkins
Sr. Vice President
and General Counsel

Attachment

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C.

Form 19b-4

Proposed Rule Change

by

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) under the Securities Exchange Act of 1934 ("Act"), NASD Regulation, Inc. ("NASD Regulation") is filing with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule change to amend Rule 2520 of the Rules of the National Association of Securities Dealers, Inc. ("NASD" or "Association") relating to margin for exempted borrowers, good faith accounts, joint back office arrangements and options transactions. The text of the proposed rule change is set forth in Exhibit 2. Proposed new language is underlined; proposed deletions are in brackets.

2. Procedures of the Self-Regulatory Organization

(a) The proposed rule change was approved by the Board of Directors of NASD Regulation at its meeting on December 3, 1998, which authorized the filing of the rule change with the SEC. The Nasdaq Stock Market has been provided an opportunity to consult with respect to the proposed rule change, pursuant to the Plan of Allocation and Delegation of Functions by the NASD to its Subsidiaries. The NASD Board of Governors had an opportunity to review the proposed rule change at its meeting on December 10, 1998. No other action by the NASD is necessary for the filing of the proposed rule change. Section 1(a)(ii) of Article VII of the NASD By-Laws permits the NASD Board of Governors to adopt amendments to NASD Rules without recourse to the membership for approval.

The NASD will announce the effective date of the proposed rule change in a Notice to Members to be published no later than 60 days following Commission approval. The effective date will be 30 days following publication of the Notice to Members announcing Commission approval.

Questions regarding this rule filing may be directed to Elliott R. Curzon, Assistant General Counsel, NASD Regulation, Office of General Counsel, at (202) 728-8451.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) **Description of Purpose and Provisions of Proposed Rule Change**

NASD Regulation is proposing to adopt amendments to the NASD's margin rule (Rule 2520) relating to exempted borrowers, good faith accounts, joint back office arrangements and options transactions, to conform to the New York Stock Exchange's (NYSE) recent changes to NYSE Rule 431 and to conform it to recently adopted changes to Regulation T promulgated by the Board of Governors of the Federal Reserve System (Federal Reserve Board). NASD Regulation is also proposing other minor changes to eliminate obsolete provisions and correct errors in the text of the Rule.

Margin Requirements for Exempted Borrowers and Good Faith Accounts

Under the recent changes to Regulation T, the Federal Reserve Board has created a new category of account called the "good faith account" to replace the "non-purpose," "arbitrage" and "government securities" accounts. In the good faith account, a customer can purchase certain securities (exempted and non-equity securities, and money market 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 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. These changes to Regulation T represent a continuing philosophical shift away from

government mandated credit regulation and toward greater reliance on industry self-regulation and risk assessment.

NASD Regulation believes that transactions in good faith accounts raise the same safety and soundness questions as transactions in cash and margin accounts. Accordingly, the proposed amendments require all accounts (except for cash accounts) to maintain margin as required by Rule 2520. Cash accounts will continue to be subject only to certain specific requirements, not the overall requirements of the Rule.

In addition, the Federal Reserve Board exempted a class of borrowers called “exempted borrowers” (broker/dealers that do substantial public business) from the requirements of Reg T. While the proposed amendments will recognize the exemption adopted by the Federal Reserve Board (by codifying the exemption in the definition of “customer” in paragraph 2520(a)(3)), they will, nevertheless, require that the proprietary accounts of an introducing member that are carried or cleared by another member remain subject to the equity requirements of 2520(e)(6), which prohibit a member from carrying a proprietary account in a deficit equity condition and require the difference between the account equity and the margin required by 2520 to be deducted from the member’s net capital.¹

¹ Under the National Securities Markets Improvement Act of 1996 (NSMIA), the Federal Reserve Board no longer has any authority to regulate credit for the market making transactions of a registered market maker (transactional exemption); however, broker/dealers that are not market makers and that do not qualify as exempted borrowers because they don’t meet the Regulation T definition are treated like ordinary customers for purposes of Regulation T initial margin. Currently, Rule 2520 permits good faith maintenance margin for broker/dealer’s market making and proprietary accounts. See Rule 2520(e)(5) and (e)(6). This good faith maintenance margin standard will not be changed under the proposed amendments.

Amendments to Provide for Joint Back Office Arrangements

NASD Regulation is also proposing amendments to provide for “joint back-office arrangements” (JBO arrangements) established pursuant to Section 220.7 of Regulation T. A joint back office arrangement is one in which the creditor is a clearing or servicing broker/dealer owned jointly or individually by other creditors.² The amendments require members, prior to establishing a JBO arrangement, to notify the Association. In addition, clearing firms in such arrangements must maintain minimum net capital of \$25 million. If the clearing firm only clears options market-maker accounts, it must maintain minimum net capital of \$7 million.

Thus, a clearing firm in a JBO arrangement must include in its ratio of gross options market maker haircuts for net capital purposes the gross deductions of JBO participant accounts. In the event that a member’s tentative net capital or net capital falls below the requirements, the firm must notify the Association of the deficiency and resolve the deficiency within three business days. If the deficiency is not resolved the member may not permit any new transactions under the JBO arrangement. In addition a clearing firm in such an arrangement must maintain a written risk analysis methodology for assessing credit extensions and deduct the excess equity of participating broker/dealers from its net capital haircuts.

A participating broker/dealer must be registered as a broker/dealer, maintain an ownership interest in the clearing member, and have a liquidating equity of \$1 million in the JBO arrangement, exclusive of its ownership interest in the clearing member.

Amendments to Margin Rules Governing Options Transactions

NASD Regulation is proposing to amend paragraph (f)(2) to add subparagraphs (L) and (M), which are identical to new provisions in NYSE Rule 431, to permit customers to designate securities positions to margin options trades, and to permit options transactions in customer cash accounts to the extent the transaction is permissible under Regulation T, or that has certain other specific characteristics.

Amendments to Conform to Changes to Regulation T

NASD Regulation is also proposing to amend Rule 2520 to conform references to Regulation T to the amendments to Regulation T recently adopted by the Federal Reserve Board.

Miscellaneous Amendments

Finally, NASD Regulation is proposing to eliminate Paragraph (c)(5) prescribing maintenance margin for American Stock Exchange Emerging Company Marketplace securities because the Emerging Company Marketplace no longer exists.

(b) Statutory Basis

NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that the Association's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The NASD believes that the proposed amendments to Rule will serve the public interest .

² See Regulation T, Section 220.7(c).

4. Self-Regulatory Organization's Statement on Burden on Competition

NASD Regulation does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

6. Extension of Time Period for Commission Action

NASD Regulation does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

The provisions of the proposed rule change relating to exempted borrowers and good faith accounts are based upon amendments to NYSE Rule 431 recently approved by the SEC in Exchange Act Release No. 34-40529 (October 7, 1998); 63 F.R. 55667 (October 16, 1998). The provisions of the proposed rule change relating to options transactions are based on provisions which were added to NYSE Rule 431 in 1997. The provisions of the proposed rule change relating to joint back-office arrangements are based on provisions included in Amendment No. 2 to SR-NYSE-97-28, submitted to the SEC on September 25, 1998.

NASD Regulation believes it is important that the NASD's and the NYSE's margin rules remain as nearly identical as possible in order to avoid imposing confusing or inconsistent margin requirements on the securities industry.

9. Exhibits

1. Completed notice of proposed rule change for publication in the Federal Register
2. Proposed amendments to the margin rule.

Pursuant to the requirements of the Securities Exchange Act of 1934, NASD Regulation has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

NASD REGULATION, INC.

BY: _____
Alden S. Adkins,
Sr. Vice President and General Counsel

Date: (Insert date)

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-NASD-99-05)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Margin for Exempted Borrowers, Good Faith Accounts, Joint Back Office Arrangements and Options Transactions

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on , NASD Regulation, Inc. ("NASD Regulation") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD Regulation. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE TERMS OF SUBSTANCE OF THE PROPOSED RULE CHANGE

NASD Regulation is proposing to amend Rule 2520 of the Rules of the National Association of Securities Dealers, Inc. ("NASD" or "Association") relating to margin for exempted borrowers, good faith accounts, joint back office arrangements and options transactions. The text of the proposed rule change is set forth in Exhibit 2 attached to the rule filing.

II. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE PURPOSE OF, AND STATUTORY BASIS FOR, THE PROPOSED RULE CHANGE

In its filing with the Commission, NASD Regulation included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it

received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. NASD Regulation has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

(A) Self-Regulatory Organization's Statement the Purpose of, and Statutory Basis for, the Proposed Rule Change

NASD Regulation is proposing to adopt amendments to the NASD's margin rule (Rule 2520) relating to exempted borrowers, good faith accounts, joint back office arrangements and options transactions, to conform to the New York Stock Exchange's (NYSE) recent changes to NYSE Rule 431 and to conform it to recently adopted changes to Regulation T promulgated by the Board of Governors of the Federal Reserve System (Federal Reserve Board). NASD Regulation is also proposing other minor changes to eliminate obsolete provisions and correct errors in the text of the Rule.

Margin Requirements for Exempted Borrowers and Good Faith Accounts

Under the recent changes to Regulation T, the Federal Reserve Board has created a new category of account called the "good faith account" to replace the "non-purpose," "arbitrage" and "government securities" accounts. In the good faith account, a customer can purchase certain securities (exempted and non-equity securities, and money market 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 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. These changes to Regulation T represent a continuing philosophical shift away from

government mandated credit regulation and toward greater reliance on industry self-regulation and risk assessment.

NASD Regulation believes that transactions in good faith accounts raise the same safety and soundness questions as transactions in cash and margin accounts. Accordingly, the proposed amendments require all accounts (except for cash accounts) to maintain margin as required by Rule 2520. Cash accounts will continue to be subject only to certain specific requirements, not the overall requirements of the Rule.

In addition, the Federal Reserve Board exempted a class of borrowers called “exempted borrowers” (broker/dealers that do substantial public business) from the requirements of Reg T. While the proposed amendments will recognize the exemption adopted by the Federal Reserve Board (by codifying the exemption in the definition of “customer” in paragraph 2520(a)(3)), they will, nevertheless, require that the proprietary accounts of an introducing member that are carried or cleared by another member remain subject to the equity requirements of 2520(e)(6), which prohibit a member from carrying a proprietary account in a deficit equity condition and require the difference between the account equity and the margin required by 2520 to be deducted from the member’s net capital.³

³ Under the National Securities Markets Improvement Act of 1996 (NSMIA), the Federal Reserve Board no longer has any authority to regulate credit for the market making transactions of a registered market maker (transactional exemption); however, broker/dealers that are not market makers and that do not qualify as exempted borrowers because they don’t meet the Regulation T definition are treated like ordinary customers for purposes of Regulation T initial margin. Currently, Rule 2520 permits good faith maintenance margin for broker/dealer’s market making and proprietary accounts. See Rule 2520(e)(5) and (e)(6). This good faith maintenance margin standard will not be changed under the proposed amendments.

Amendments to Provide for Joint Back Office Arrangements

NASD Regulation is also proposing amendments to provide for “joint back-office arrangements” (JBO arrangements) established pursuant to Section 220.7 of Regulation T. A joint back office arrangement is one in which the creditor is a clearing or servicing broker/dealer owned jointly or individually by other creditors.⁴ The amendments require members, prior to establishing a JBO arrangement, to notify the Association. In addition, clearing firms in such arrangements must maintain minimum net capital of \$25 million. If the clearing firm only clears options market-maker accounts, it must maintain minimum net capital of \$7 million.

Thus, a clearing firm in a JBO arrangement must include in its ratio of gross options market maker haircuts for net capital purposes the gross deductions of JBO participant accounts. In the event that a member’s tentative net capital or net capital falls below the requirements, the firm must notify the Association of the deficiency and resolve the deficiency within three business days. If the deficiency is not resolved the member may not permit any new transactions under the JBO arrangement. In addition a clearing firm in such an arrangement must maintain a written risk analysis methodology for assessing credit extensions and deduct the excess equity of participating broker/dealers from its net capital haircuts.

A participating broker/dealer must be registered as a broker/dealer, maintain an ownership interest in the clearing member, and have a liquidating equity of \$1 million in the JBO arrangement, exclusive of its ownership interest in the clearing member.

Amendments to Margin Rules Governing Options Transactions

NASD Regulation is proposing to amend paragraph (f)(2) to add subparagraphs (L) and (M), which are identical to new provisions in NYSE Rule 431, to permit customers to designate securities positions to margin options trades, and to permit options transactions in customer cash accounts to the extent the transaction is permissible under Regulation T, or that has certain other specific characteristics.

Amendments to Conform to Changes to Regulation T

NASD Regulation is also proposing to amend Rule 2520 to conform references to Regulation T to the amendments to Regulation T recently adopted by the Federal Reserve Board.

Miscellaneous Amendments

Finally, NASD Regulation is proposing to eliminate Paragraph (c)(5) prescribing maintenance margin for American Stock Exchange Emerging Company Marketplace securities because the Emerging Company Marketplace no longer exists.

NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that the Association's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The NASD believes that the proposed amendments to Rule will serve the public interest .

⁴ See Regulation T, Section 220.7(c).

(B) Self-Regulatory Organization's Statement on Burden on Competition

NASD Regulation does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. DATE OF EFFECTIVENESS OF THE PROPOSED RULE CHANGE AND TIMING FOR COMMISSION ACTION

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

A. by order approve such proposed rule change, or

B. institute proceedings to determine whether the proposed rule change should be disapproved.

IV. SOLICITATION OF COMMENTS

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission

and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to the file number in the caption above and should be submitted by [insert date 21 days from the date of publication].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Jonathan G. Katz
Secretary

EXHIBIT 2

PROPOSED AMENDMENTS TO THE MARGIN RULE

(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) The term "basket" shall mean a group of stocks that the Association or any national securities exchange designates as eligible for execution in a single trade through its trading facilities and that consists of stocks whose inclusion and relative representation in the group are determined by the inclusion and relative representation of their current market prices in a widely-disseminated stock index reflecting the stock market as a whole.

(2) The term "current market value" means the total cost or net proceeds of a security on the day it was purchased or sold or at any other time the preceding business day's closing price as shown by any regularly published reporting or quotation service. If there is no closing price, a member may use a reasonable estimate of the market value of the security as of the close of business on the preceding business day.

(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) The term "designated account" means the account of a bank, trust company, insurance company, investment trust, state or political subdivision thereof, charitable or nonprofit educational institution regulated under the laws of the United States or any state, or pension or profit sharing plan subject to ERISA or of any agency of the United States or of a state or a political subdivision thereof.

(5) The term "equity" means the customer's ownership interest in the account, computed by adding the current market value of all securities "long" and the amount of any credit balance and subtracting the current market value of all securities "short" and the amount of any debit balance.

(6) The term "exempted security" or "exempted securities" has the meaning as in Section 3(a)(12) of the Act.

(7) The term "margin" means the amount of equity to be maintained on a security position held or carried in an account.

(8) The term "person" has the meaning as in Section 3(a)(9) of the Act.

(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 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) Additional Margin

Procedures shall be established by members to:

(1) review limits and types of credit extended to all customers;

(2) formulate their own margin requirements; and

(3) review the need for instituting higher margin requirements, mark-to- markets and collateral deposits than are required by this paragraph for individual securities or customer accounts.

(e) Exceptions to Rule

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

(1) Offsetting "Long" and "Short" Positions

When a security carried in a "long" position is exchangeable or convertible within a reasonable time, without restriction other than the payment of money, into a security carried in a "short" position for the same customer, the margin to be maintained on such positions shall be 10 percent of the current market value of the "long" securities. When the same security is carried "long" and "short" the margin to be maintained on such positions shall be 5 percent of the current market value of the "long" securities. In determining such margin requirements "short" positions shall be marked to the market.

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

(A) Obligations of the United States

On net "long" or net "short" positions in obligations (including zero coupon bonds, i.e., bonds with coupons detached or non-interest bearing bonds) issued or guaranteed as to principal or interest by the United States Government or issued or guaranteed by corporations in which the United States has a direct or indirect interest as shall be designated for exemption by the Secretary of the Treasury, the margin to be maintained shall be the percentage of the current market value of such obligations as specified in the applicable category below:

(i)	Less than one year to maturity	1 percent
(ii)	One year but less than three years to maturity	2 percent
(iii)	Three years but less than five years to maturity	3 percent
(iv)	Five years but less than ten years to maturity	4 percent
(v)	Ten years but less than twenty years to maturity,	5 percent, or
(vi)	Twenty years or more to maturity	6 percent

Notwithstanding the above, on zero coupon bonds with five years or more to maturity the margin to be maintained shall not be less than 3 percent of the principal amount of the obligation.

When such obligations other than United States Treasury bills are due to mature in thirty calendar days or less, a member, at its discretion, may permit the customer to substitute another such obligation for the maturing obligation and use the margin held on the maturing obligation to reduce the margin required on the new obligation, provided the customer has given the member irrevocable instructions to redeem the maturing obligation.

(B) All Other Exempted Securities

On any positions in exempted securities other than obligations of the United States, the margin to be maintained shall be 15 percent of the current market value or 7 percent of the principal amount of such obligation, whichever amount is greater.

(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) Baskets

Notwithstanding the other provisions of this Rule, a member may clear and carry basket transactions of one or more members registered as market makers (who are deemed specialists for purposes of Section 7 of the Act pursuant to the rules of a national securities exchange) upon a margin basis satisfactory to the concerned parties, provided all real and potential risks in accounts carried under such arrangements are at all times adequately covered by the margin maintained in the account or, in the absence thereof, by the carrying member when computing net capital under SEC Rule 15c3-1.

(E) Special Provisions

Notwithstanding the foregoing in this paragraph (e)(2):

(i) A member may, at its discretion, permit the use of accrued interest as an offset to the maintenance margin required to be maintained; and

(ii) The Association upon written application, may permit lower margin requirements on a case-by-case basis.

(F) Cash Transactions With Customers

When a customer purchases an issued exempted security from or through a member in a cash account, full payment shall be made promptly. If, however, delivery or payment therefor is not made promptly after the trade date, a deposit shall be required as if it were a margin transaction, unless it is a transaction with a "designated account."

On any position resulting from a transaction in issued exempted securities made for a member, or a non-member broker/dealer, or made for or with a "designated account," no margin need be required and such position need not be marked to the market. However, where such 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.

(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) International Arbitrage Accounts
- International arbitrage accounts for non-member foreign brokers or dealers who are members of a foreign securities exchange shall not be subject to this paragraph. The amount of any deficiency between the equity in such an account and the margin required by the other provisions of this paragraph shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

(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 Offices 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; (a) promptly notify the Association in writing

of such deficiency, (b) 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 220.11; and

c. maintain a minimum liquidating equity of \$1 million in the JBO arrangement exclusive of the ownership interest established in (2) 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 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.

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) Shelf-Registered Securities - The equity to be maintained in margin accounts of customers for securities which are the subject of a current and effective registration for a delayed offering (shelf-registered securities) shall be at least the amount of margin required by paragraph (c)(3) provided the member:

- (i) obtains a current prospectus in effect with the Commission, meeting the requirements of Section 10 of the Securities Act of 1933, covering such securities;
- (ii) has no reason to believe the Registration Statement is not in effect or that the issuer has been delinquent in filing such periodic reports as may be required of it with the Commission and is satisfied that such registration will be kept in effect and that the prospectus will be maintained on a current basis; and
- (iii) retains a copy of such Registration Statement, including the prospectus, in an easily accessible place in its files.

Shelf-registered securities which do not meet all the conditions prescribed above shall have no value for purposes of this paragraph (c). Also see subparagraph (C) below.

(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 (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) makes volume computations necessary to determine the amount of securities then salable under Rule 144 or 145(d) under the Securities Act of 1933 on a weekly basis or at such frequency as the member and/or the Association may deem appropriate under the circumstances. See also subparagraph (C) below.

(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 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:

Percent of Outstanding Shares	or, Percent of Average Weekly Volume	Margin Requirement
Up to 10 percent	Up to 100 percent	25 percent
Over 10 percent and under 15 percent	Over 100 percent and under 200 percent	30 percent
15 percent and under 20 percent	Over 200 percent and under 300 percent	45 percent
20 percent and under 25 percent	300 percent and under 400 percent	60 percent
25 percent and under 30 percent	400 percent and under 500 percent	75 percent
30 percent and above	500 percent and above	100 percent

For purposes of this sub-paragraph (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), 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) Determination of Value for Margin Purposes

Active securities dealt in on a national securities exchange or OTC Marginable securities listed on Nasdaq shall, for margin purposes, be valued at current market prices. Other securities shall be valued conservatively in view of current market prices and the amount which might be realized upon liquidation. Substantial additional margin must be required in all cases where the securities carried in "long" or "short" positions are subject to unusually rapid or violent changes in value, or do not have an active market on Nasdaq or on a national securities exchange, or where the amount carried is such that the position(s) cannot be liquidated promptly.

(2) Puts, Calls and Other Options

(A) Except as provided below, no put or call carried for a customer shall be considered of any value for the purpose of computing the margin to be maintained in the account of such customer.

(B) The issuance, guarantee or sale (other than a "long" sale) for a customer of a put or a call shall be considered a security transaction subject to paragraph (c)(2).

(C) For purposes of this subparagraph (6)(B), obligations issued by the United States Government shall be referred to as United States Government obligations. Mortgage pass-through obligations guaranteed as to timely payment of principal and interest by the Government National Mortgage Association shall be referred to as GNMA obligations. The terms "current market value" or "current market price" of an option shall mean the total cost or net proceeds of the option contract on the day the option was purchased or sold and at any other time shall be the preceding business day's closing price of that option (times the appropriate unit of trading or multiplier) as shown by any regularly published reporting or quotation service. The term "exercise settlement amount" shall mean the difference between the "aggregate exercise price"

and the "aggregate current index value" (as such terms are defined in the pertinent By-Laws of The Options Clearing Corporation).

(D) The margin required on any put or call issued, guaranteed or carried "short" in a customer's account shall be:

(i) In the case of puts and calls issued by a registered clearing agency, 100 percent of the current market value of the option plus the percentage of the current market value of the underlying security or index specified in column II of the chart below. Notwithstanding the margin required below, the minimum margin on any put or call issued, guaranteed or carried "short" in a customer's account may be reduced by any "out-of-the-money amount" (as defined below), but shall not be less than 100 percent of the current market value of the option plus the percentage of the current market value of the underlying security or index specified in column III.

	I Security or Index	II Initial and/or Maintenance Margin Required	III Minimum Margin Required	IV Underlying Component Value
1	Stock	20 percent	10 percent	The equivalent number of shares at current market prices.
2	Industry index stock group	20 percent	10 percent	The product of the current index group value and the applicable index multiplier.
3	Broad index stock group	15 percent	10 percent	The product of the current index group value and the applicable index multiplier.
4	U.S Treasury bills-95 days or less to maturity	.35 percent	1/20 percent	The underlying principle amount.
5	U.S Treasury notes	3 percent	1/2 percent	The underlying principle amount.
6	U.S Treasury bonds	3.5 percent	1/2 percent	The underlying principle amount.
7	Foreign Currencies	4 percent	3/4 percent	The product of units per foreign currency contract and the closing spot price.

8	Interest Rate contracts	10 percent	5 percent	The product of the current interest rate measure and the applicable multiplier.
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For purposes hereof, "out-of-the-money amounts" are determined as follows:

Options Issue	Call	Put
Stock Options	Any excess of the aggregate exercise price of the option over the current market value of the equivalent number of shares of the underlying security.	Any excess of the current market value of the equivalent number of shares of the underlying security over the aggregate exercise price of the option.
U.S. Treasury Options	Any excess of the aggregate exercise price of the option over the current market value of the underlying principle amount.	Any excess of the current market value of the underlying principle amount over the aggregate exercise price of the option.
Index Stock Group Options	Any excess of the aggregate exercise price of the option over the product of the current index group value and the applicable multiplier.	Any excess of the product of the current index group value and the applicable multiplier over the aggregate exercise price of the option.
Foreign Currency Options	Any excess of the aggregate exercise price of the option over the product of units per foreign currency contract and the closing spot price.	The product of units per foreign currency contract and the closing spot prices over the aggregate price of the option.
Interest Rate Options	Any excess of the aggregate exercise price of the option over the product of the current interest rate measure value and the applicable multiplier.	Any excess of the product of the current interest rate measure value and the applicable multiplier over the aggregate exercise price of the option.

If the option contract provides for the delivery of obligations with different maturity dates or coupon rates, the computation of the "out-of-the-money amount," if any, where required by this Rule, shall be made in such a manner as to result in the highest margin requirement on the short option position.

(ii) In the case of puts and calls issued by a registered clearing agency which represent options on GNMA obligations in the principal amount of \$100,000, 130 percent of the current market value of the option plus \$1,500, except that the margin required need not exceed \$5,000 plus the current market value of the option.

(iii) In the case of puts and calls not issued by a registered clearing agency the percentage of the current value of the underlying component and the applicable multiplier, if any, specified in column II below, plus any "in-the-money amount" (as defined in this paragraph (f)(2)(D)(iii)).

Notwithstanding the margin required by this subparagraph, the minimum margin on any put or call issued, guaranteed or carried "short" in a customer's account may be reduced by any "out of the money amount" (as defined in paragraph (f)(2)(D)(i)), but shall not be less than the percentage of the current value of the underlying component and the applicable multiplier, if any, specified in column III below.

	I Type of Option	II Initial and/or Maintenance Margin Required	III Minimum Margin Required	IV Underlying Component Value
1	Stock and convertible corporate debt securities	30%	10%	The equivalent number of shares at current market prices for stocks or the underlying principal amount for convertible corporate debt securities.
2	Industry Index stock group	30%	10%	The product of the current index group value and the applicable index multiplier.
3	Broad index stock group	20%	10%	The product of the current index group value and the applicable index multiplier.
4	U.S. Government or U.S. Government Agency debt Securities other than those exempted by Rule 3a12-7 under the Securities Exchange Act of 1934*	5%	3%	The underlying principle amount.

5	Corporate debt securities registered on a national securities exchange and marginable OTC corporate debt securities as defined in Regulation T Section 220.2(t)(1)**	15%	5%	The underlying principle amount.
6	All other OTC options not covered above	45%	20%	The underlying principle amount.

For the purpose of this subparagraph (f)(2)(D)(iii), "in-the-money amounts" are determined as follows:

Option Issue	Call	Put
Stock options	Any excess of the current market value of the equivalent number of shares of the underlying security over the aggregate exercise price of the option.	Any excess of the aggregate exercise price of the option over the current market value of the equivalent number of shares of the underlying security.
Index stock group options	Any excess of the product of the current index group value and the applicable multiplier over the aggregate exercise price of the option.	Any excess of the product of the aggregate exercise price of the option over the product of the current index group value and the applicable multiplier.
U.S. Government mortgage related or corporate debt securities options	Any excess of the current value of the underlying principal amount over the aggregate exercise price of the option.	Any excess of the aggregate exercise price of the option over the current value of the underlying principal amount.

(iv) Puts and calls not issued by a registered clearing agency and representing options on U.S. Government and U.S. Government Agency debt securities that qualify for exemption pursuant to Rule 3a12-7 under the Act, must be for a principal amount of not less than \$500,000, and shall be subject to the following requirements:

- a. For exempt accounts, 3% of the current value of the underlying principal amount on thirty (30) year U.S. Treasury bonds and non-mortgage backed U.S. Government agency debt securities; and 2% of the current value of the underlying

principal amount on all other U.S. Government and U.S. Government agency debt securities, plus any "in-the-money amount" (as defined in (f)(2)(D)(iii)) or minus any "out-of-the-money amount" (as defined in (f)(2)(D)(i)). The amount of any deficiency between the equity in the account and the margin required shall be deducted in computing the net capital of the member under the SEC's net capital Requirements on the following basis:

1. On any one account or group of commonly controlled accounts to the extent such deficiency exceeds 5% of a member's tentative net capital (net capital before haircuts), 100% of such excess amount, and
 2. On all accounts combined to the extent such deficiency exceeds 25% of a member's tentative net capital, 100% of such excess amount, reduced by any amount already deducted pursuant to (a) above.
- b. For non-exempt accounts, 5% of the current value of the underlying principal amount on thirty (30) year U.S. Treasury bonds and non-mortgage backed U.S. Government agency debt securities; and 3% of the current value of the underlying principal amount on all other U.S. Government and U.S. Government agency debt securities, plus any "in-the-money amount" or minus any "out-of-the-money amount", provided the minimum margin shall not be less than 1% of the current value of the underlying principal amount.

For purposes of this subsection (f)(2)(D)(iv), an "exempt account" shall be defined as a member, non-member broker/dealer, "designated account", any person having net tangible assets of at least sixteen million dollars or in the case of mortgage-related debt securities transactions an independently audited mortgage banker with both more than \$1.5 million of net current assets (which may include 3/4 of 1% maximum allowance on loan servicing portfolios) and with more than \$1.5 million of net worth.

(E)

(i) Each put or call shall be margined separately and any difference between the current market value of the underlying component and the exercise price of a put or call shall be considered to be of value only in providing the amount of margin required on that particular put or call. Substantial additional margin must be required on options issued, guaranteed or carried "short" with an usually long period of time to expiration, or written on securities which are subject to unusually rapid or violent changes in value, or which do not have an active market, or where the securities subject to the option cannot be liquidated promptly.

(ii) No margin need be required on any "covered" put or call.

(F)

(i) Where both a put and call specify the same underlying component are issued by a registered clearing agency and are carried "short" for a customer, the amount of margin required shall be the margin on the put or call, whichever is greater, as required pursuant to subparagraph (f)(2)(D)(i) above, plus the current market value on the other option.

(ii) Where either or both the put and call specifying the same underlying component are not issued by a registered clearing agency and are issued, guaranteed or carried "short" for a customer by the same broker-dealer (as defined in subparagraph (f)(2)(G)(iii) below), the amount of margin required shall be the margin on the put or call, whichever is greater, as required pursuant to subparagraph (f)(2)(D)(iii) and (D)(iv) above, plus any unrealized loss on the other option. Where either or both the put or call are not issued, guaranteed or carried by the same broker/dealer then the put and call must be margined separately pursuant to subparagraph (f)(2)(D)(iii) and (D)(iv) above, however, the minimum margin shall not apply to the other option.

(iii) If both a put and call for the same GNMA obligation in the principal amount of \$100,000 are issued, guaranteed or carried "short" for a customer, the amount of margin required shall be the margin on the put or call, whichever is greater, as required pursuant to subparagraph (f)(2)(D)(ii) above, plus the current market value of the other option.

(G)

(i) Where a call that is issued by a registered clearing agency is carried "long" for a customer's account and the account is also "short" a call issued by a registered clearing agency, expiring on or before the date of expiration of the "long" listed call and specifying the same underlying component the margin required on the "short" call shall be the lower of:

- a. the margin required pursuant to subparagraph (f)(2)(D)(i) above; or
- b. the amount, if any, by which the exercise price of the "long" call exceeds the exercise price of the "short" call.

(ii) Where a put that is issued by a registered clearing agency is carried "long" for a customer's account and the account is also "short" a put issued by a registered clearing agency, expiring on or before the date of expiration of the "long" listed put and specifying the same underlying component the margin required on the "short" put shall be the lower of:

a. the margin required pursuant to subparagraph (f)(2)(D)(i) above, in the case of stock options, United States Government obligations, foreign currency options or index stock group options; or

b. the amount, if any, by which the exercise price of the "short" put exceeds the exercise price of the "long" put.

(iii)

a. Where a call that is issued by a registered clearing agency is carried "long" for a customer's account and the account is also "short" a call issued by a registered clearing agency, expiring on or before the date of expiration of the "long" listed call and written on the same GNMA obligation in the principal amount of \$100,000, the margin required on the "short" call shall be the lower of:

1. the margin required pursuant to subparagraph (f)(2)(D)(ii) above; or
2. the amount, if any, by which the exercise price of the "long" call exceeds the exercise price of the "short" call multiplied by the appropriate multiplier factor set forth below.

b. Where a put that is issued by a registered clearing agency is carried "long" for a customer's account and the account is also "short" a put issued by a registered clearing agency, expiring on or before the date of expiration of the "long" listed put and written on the same GNMA obligation in the principal amount of \$100,000, the margin required on the "short" put shall be the lower of:

3. the margin required pursuant to subparagraph (f)(2)(D)(ii) above; or
4. the amount, if any, by which the exercise price of the "short" put exceeds the exercise price of the "long" put multiplied by the appropriate multiplier factor set forth below.

c. For purposes of this subparagraph (f)(2)(G)(iii) the multiplier factor to be applied shall depend on the then current highest qualifying rate as defined by the rules of the national securities exchange or national securities association on or through which the option is listed or traded. If the then current highest qualifying rate is less than 8 percent, the multiplier factor shall be 1; if the then current highest qualifying rate is greater than or equal to 8 percent but less than 10 percent, the multiplier factor shall be 1.2; if the then current highest qualifying rate is greater than or equal to 10 percent but less than 12 percent, the multiplier factor shall be 1.4; if the then current highest qualifying rate is greater than or equal to 12 percent but less than 14 percent, the multiplier factor shall be 1.5; if the then current highest qualifying rate is greater than or equal to 14 percent but

less than 16 percent, the multiplier factor shall be 1.6; and if the then current highest qualifying rate is greater than or equal to 16 percent but less than or equal to 18 percent, the multiplier factor shall be 1.7. The multiplier factor or factors for higher qualifying rates shall be established by the Association as required.

(iii)

a. Where a call that is issued by a broker/dealer is carried "long" for a customer's account and the account is also "short" a call issued by the same broker/dealer, expiring on or before the date of expiration of the "long" call and specifying the same underlying component, the margin required on the short "call" shall be the lower of:

1. the margin required pursuant to subparagraph (f)(2)(D)(iii) or (D)(iv) above; or
2. the amount, if any, by which the exercise price of the "long" call exceeds the exercise price of the "short" call.

b. Where a put that is issued by a broker/dealer is carried "long" for a customer's account and the account is "short" a put issued by the same broker/dealer, expiring on or before the date of expiration of the "long" put and specifying the same underlying component, the margin required on the "short" put shall be the lower of:

1. the margin required pursuant to subparagraphs (f)(2)(D)(iii) or (D)(iv) above; or
2. the amount, if any, by which the exercise price of the "short" put exceeds the exercise price of the "long" put.

c. A "long" call and a "short" call or a "long" put and a "short" put are deemed to be issued by the same broker/dealer when either the broker/dealer has issued or guaranteed both options or issued or guaranteed one of the options and the other option was issued by a registered clearing agency on behalf of that broker/dealer. If the options are not issued by the same broker/dealer then the "short" put or the "short" call must be margined separately pursuant to subparagraphs (f)(2)(D)(iii) or (D)(iv) above.

(H)

(i) Where a call is issued, guaranteed or carried "short" against an existing net "long" position in the security under option or in any security immediately exchangeable or convertible, other than warrants, without restriction including the

payment of money into the security under option, no margin need be required on the call, provided:

- a. such net long position is adequately margined in accordance with this Rule and
- b. the right to exchange or convert the net "long" position does not expire on or before the date of expiration of the "short" call.

Where a put is issued, guaranteed or carried "short" against an existing net "short" position in the security under option, no margin need be required on the put, provided such net "short" position is adequately margined in accordance with this Rule.

(ii) Where a call representing stock options is issued, guaranteed or carried "short" against an existing net "long" position in a warrant convertible into the underlying security under option, margin shall be required on the call equal to any amount by which the conversion price of the "long" warrant exceeds the exercise price of the call, provided:

- a. such net long position is adequately margined in accordance with this Rule and
- b. the right to convert the net "long" position does not expire on or before the date of expiration of the "short" call. However, when a payment of money is required to convert the "long" warrant such warrant shall have no value for purposes of this Rule.

(iii) In determining net "long" and net "short" positions, for purposes of subparagraphs (f)(2)(H)(i) and (ii) above, offsetting "long" and "short" positions in exchangeable or convertible securities (including warrants) or in the same security, as discussed in paragraph (c)(5)(A), shall be deducted. In computing margin on such an existing net security position carried against a put or call, the current market price to be used shall not be greater than the exercise price in the case of a call or less than the current market price in the case of a put and the required margin shall be increased by any unrealized loss.

(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].

(I) When a member issues or guarantees an option to receive or deliver securities or foreign currencies for a customer, such option shall be margined as if it were a put or call.

(J)

(i) Registered specialists, market makers or traders - Notwithstanding the other provisions of this subparagraph (f)(2), a member may clear and carry the listed option transactions of one or more registered specialists, registered market makers or registered traders in options (which registered traders are deemed specialists for

all purposes under the Act, pursuant to the rules of a national securities exchange) (hereinafter referred to as "specialist(s)"), upon a "Good Faith" margin basis satisfactory to the concerned parties, provided the "Good Faith" margin requirements is not less than the net capital haircut deduction of the member carrying the transaction pursuant to SEC Rule 15c3-1 under the Act. In Lieu of collecting the "Good Faith" margin requirement, a carrying member may elect to deduct in computing its net capital the amount of any deficiency between the equity maintained in the account and the "Good Faith" margin required.

For purposes of this paragraph (f)(2)(J), a permitted offset position means, in the case of an option in which a specialist makes a market, a position in the underlying asset or other related assets, and in the case of other securities in which a specialist makes a market, a position in options overlying the securities in which a specialist makes a market. Accordingly, a specialist in options may establish on a share-for-share basis, a long or short position in the securities underlying the options in which the specialist makes a market, and a specialist in securities other than options may purchase or write options overlying the securities in which the specialist makes a market, if the account holds the following permitted offset positions:

- a. A short option position which is "in or at the money" and is not offset by a long or short option position for an equal or greater number of shares of the same underlying security which is "in the money";
- b. A long option position which is "in or at the money" and is not offset by a long or short option position for an equal or greater number of shares of the same underlying security which is "in the money";
- c. A short option position against which an exercise notice was tendered;
- d. A long option position which was exercised;
- e. A net long position in a security (other than an option) in which a specialist makes a market;
- f. A net short position in a security (other than an option) in which the specialist makes a market; or
- g. A specified portfolio type as referred to in SEC Rule 15c3-1, including its appendices, or any applicable SEC staff interpretation or no-action position.

Permitted offset transactions must be effected for market making purposes such as hedging, risk reduction, rebalancing of positions, liquidation, or accommodations of customer orders, or other similar market making purpose.

For purposes of this paragraph (f)(2)(J), the term "in or at the money" means the current market price of the underlying security is not more than two standard exercise intervals below (with respect to a call option) or above (with respect to a put option) the exercise price of the option; the term "in the money" means the current market price of the underlying asset or index is not below (with respect to a call option) or above (with respect to a put option) the exercise price of the option; and, the term "overlying option" means a put option purchased or a call option written against a long position in an underlying asset; or a call option purchased or a put option written against a short position in an underlying asset.

(ii) Securities, including options, in such accounts shall be valued conservatively in the light of current market prices and the amount which might be realized upon liquidation. Substantial additional margin must be required or excess net capital maintained in all cases where the securities carried:

- a. are subject to unusually rapid or violent changes in value including volatility in the expiration months of options;
- b. do not have an active market; or
- c. in one or more or all accounts, including proprietary accounts combined, are such that they cannot be liquidated promptly or represent undue concentration of risk in view of the carrying member's net capital and its overall exposure to material loss.

(K) The Association may at any time impose higher margin requirements with respect to any option position(s) when it deems such higher margin requirements are appropriate.

(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, providing:

(i) The transaction is permissible under Regulation T, Section 220.8; or

(ii) The transaction is a debit put spread in listed broad-based index options with European-style exercise comprised of a long put(s) coupled with a short put(s) overlying the same broad-based index with an equivalent underlying aggregate index value and the short put(s) and long put(s) expire simultaneously, and the strike price of the long put(s) exceed the strike price of the short put(s).

(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) be adjusted for any unrealized loss in such "short" position.

(A) 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) 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."

(4) Guaranteed Accounts

Any account guaranteed by another account may be consolidated with such other account and the margin to be maintained may be determined on the net position of both accounts, provided the guarantee is in writing and permits the member carrying the account, without restriction, to use the money and securities in the guaranteeing account to carry the guaranteed account or to pay any deficit therein; and provided further that such guaranteeing account is not owned directly or indirectly by (i) a member, or any stockholder (other than a holder of freely transferable stock only) in the member carrying such account, or (ii) a member, or any stockholder (other than a holder of freely transferable stock only) therein having a definite arrangement for participating in the commissions earned on the guaranteed account. However, the guarantee of a limited partner or of a holder of non-voting stock, if based upon his resources other than his capital contribution to or other than his interest in a member, is not affected by the foregoing prohibition, and such a guarantee may be taken into consideration in computing margin to be maintained in the guaranteed account.

When one or more accounts are guaranteed by another account and the total margin deficiencies guaranteed by any guarantor exceeds 10 percent of the member's excess net capital, the amount of the margin deficiency being guaranteed in excess of 10 percent of excess net capital shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

(5) Consolidation of Accounts

When two or more accounts are carried for a customer, the margin to be maintained may be determined on the net position of said accounts, provided the customer has consented that the money and securities in each of such accounts may be used to carry or pay any deficit in all such accounts.

(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) 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.

(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.

(8) Special Initial and Maintenance Margin Requirements

(A) Notwithstanding the other provisions of this Rule, the Association may, whenever it shall determine that market conditions so warrant, prescribe:

- (i) higher initial margin requirements for the purpose of effecting new securities transactions and commitments in accounts of customers with respect to specific securities;
- (ii) higher maintenance margin requirements for accounts of customers with respect to any securities; and
- (iii) such other terms and conditions as the Association shall deem appropriate relating to initial and/or maintenance margin requirements for accounts of customers with respect to any securities.

(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.

(C) 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 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.

(10) Margin For Index/Currency Warrants

(A) This subparagraph (10) sets forth the minimum amount of margin which must be deposited and maintained in margin accounts of customers having positions in index warrants, currency index warrants or currency warrants dealt in on Nasdaq or a national securities exchange. The Association may at any time impose higher margin requirements in respect of such positions when it deems such higher margin requirements to be advisable. The initial deposit of margin required under this Rule must be made within five full business days after the date on which a transaction giving rise to a margin requirement is effected. The margin requirements set forth in this subparagraph (J) are applicable only to index warrants, currency index warrants and currency warrants listed for trading on Nasdaq or a national securities exchange on or after September 28, 1995.

(B) Definitions

The following definitions shall apply to transactions in index warrants, currency index warrants, and currency warrants.

(i) The term "currency call warrant" means a warrant structured as a call on the underlying currency. The term "currency put warrant" means a warrant structured as a put on the underlying currency.

(ii) The term "currency index call warrant" means a warrant structured as a call on the underlying currency index. The term "currency index put warrant" means a warrant structured as a put on the underlying currency index.

(iii) The term "current market value" of an index warrant, currency index warrant or currency warrant shall mean the total cost or net proceeds of the transaction on the day the warrant was purchased or sold and at any other time shall mean the most recent closing price of that issue of warrants on Nasdaq, in the case of a Nasdaq-listed index warrants, or the exchange on which it is listed on any day with respect to which a determination of current market value is made.

(iv) The term "index call warrant" means a warrant structured as a call on the underlying stock index group. The term "index put warrant" means a warrant structured as a put on the underlying stock index group.

(v) The term "index group value" in respect to a currency index warrant means the numerical index value of particular currency index multiplied by \$1.00 U.S. or the applicable index multiplier.

(vi) The term "index group value" in respect of an index warrant means the numerical index value of a particular stock index multiplied by \$1.00 U.S. or other applicable index multiplier.

(vii) The term "numerical index value" in respect of a currency index warrant means the level of a particular currency index as reported by the reporting authority for the index.

(viii) The term "numerical index value" in respect of an index warrant means the level of a particular stock index as reported by the reporting authority for the index.

(ix) The term "reporting authority" in respect of a currency index warrant means the institution or reporting service specified in the prospectus for the warrant as the official source for calculating and reporting the levels of such currency index.

(x) The term "reporting authority" in respect of an index warrant means the institution or reporting service specified in the prospectus for the warrant as the official source for calculating and reporting the levels of such stock index.

(xi) The term "spot price" in respect of a currency warrant on a particular business day means the noon buying rate in U.S. dollars on such day in New York City for cable transfers of the particular underlying currency as certified for customs purposes by the Federal Reserve Bank of New York.

(xii) The terms "stock index group," "index warrants," "currency warrants," "currency index," and "currency index warrants" when used in reference to an index warrant, currency index warrant, or currency warrant shall have the same meanings as set forth in Rule 2842.

(xiii) The term "strike price" in respect of an index warrant, currency index warrant or currency warrant means the price at which the warrant may be exercised in accordance with its terms.

(xiv) The term "unit of underlying currency" in respect of a currency warrant means a single unit of the currency covered by the warrant.

(C) Except as provided in this subparagraph (J), no index warrant, currency index warrant or currency warrant carried for a customer shall be considered of any value for the purpose of computing the margin required in the account of such customer. Subject to the exceptions set forth in subparagraph (J)(v) of this Rule, the minimum margin on any currency warrant, currency index warrant or index warrant issued, guaranteed or carried "short" in a customer's account shall be:

(i) In the case of an index put or call warrant, 100% of the current market value of each such warrant plus 15% of the current index group value. Such amount shall be decreased by the excess of the strike price of the warrant over the current index group value in the case of an index call warrant, or the excess of the current index group value over the strike price of the warrant in the case of an index put warrant; or

(ii) In the case of a currency put or call warrant, 100% of the current market value of each such warrant plus 4% (or such other percentage, as specified by the national securities exchange listing the warrant and approved by the Commission on a case-by-case basis) of the product of the units of underlying currency per warrant and the spot price for such currency. The add-on percentage with respect to warrants on the German Mark, French Franc, Swiss Franc, Japanese Yen, British Pound, Australian Dollar, U.S. and European Currency Unit ("ECU") shall be four percent (4%), and for the Canadian Dollar the "add-on" percentage shall be one

percent (1%). Such amount shall be decreased by the excess of the strike price of the warrant over the product of the units of underlying currency per warrant and the spot price of the currency in the case of a currency call warrant, or any excess of the product of the units of underlying currency per warrant and the spot price over the strike price of the warrant in the case of a currency put warrant; or

(iii) In the case of the currency index put or call warrants, 100% of the current market value of each such warrant plus a percentage, as specified by the national securities exchange listing the warrant and approved by the Commission on a case-by-case basis, of the current index group value. Such amount shall be decreased by the excess of the strike price of the warrant over the current index group value in the case of a currency index call warrant, or any excess of the current index group value over the strike price of the warrant in the case of a currency index put warrant.

Notwithstanding the foregoing:

(D) The minimum margin on each currency put or call warrant, currency index put or call warrant or index put or call warrant issued, guaranteed or carried "short" in a customer's account shall be not less than 100% of the current market value of such warrant plus:

(i) 10% of the current index group value in the case of an index warrant;

(ii) .75% (.0075) (or such other percentage as specified by the national securities exchange listing the warrant and approved by the Commission) of the product of the units of underlying currency per warrant and the spot price of such currency, in the case of a currency warrant; or

(iii) in the case of currency index warrants, a percentage of the current index group value as specified by the national securities exchange listing the warrant and approved by the Commission.

(E)

(i) When a "short" position in an index call warrant, currency index call warrant or currency call warrant is offset by a "short" position of equivalent underlying value in a put warrant or a put option issued by The Options Clearing Corporation on the same index or currency, or a "short" position in an index put warrant, currency index put warrant or currency put warrant is offset by a "short" position of equivalent underlying value in a call warrant or a call option issued by The Options Clearing Corporation on the same index or currency, the margin required shall be the margin on the put position or the call position, whichever is greater, plus the current market value of the other position.

(ii) When a "long" position in an index call warrant, currency index call warrant or currency call warrant is offset by a "short" position of equivalent underlying value in a call warrant or a call option issued by The Options Clearing Corporation on the same index or currency, then, provided that the "long" position expires no earlier than the "short" position, the margin required shall be the amount, if any, by which the strike price of the "long" position exceeds the strike price of the "short" position.

(iii) When a "long" position in an index put warrant, currency index put warrant or currency put warrant is offset with a "short" position of equivalent underlying value in a put warrant or a put option issued by The Option Clearing Corporation on the same index or currency, then, provided that the "long" position expires no earlier than the "short" position, the margin required shall be the amount, if any, by which the strike price of the "short" position exceeds the strike price of the "long" position.

(iv) The margin treatment for spread positions pursuant to subparagraphs (iii)a., b., and c. above is subject to a one-year pilot program scheduled to begin September 28, 1995.

(v) No margin is required in respect of a "short" position in an index call warrant where the customer has delivered, promptly after the warrant has been sold short, to the member with which such position is maintained, a Market Index Warrant Escrow Receipt in a form satisfactory to the Association, issued by a bank or trust company pursuant to specific authorization from the customer which certifies that the issuer of the agreement holds for the account of the customer:

- a. cash;
- b. cash equivalents;
- c. one or more qualified equity securities; or
- d. a combination thereof;

that such deposit has an aggregate market value, at the time the warrant is sold short, of not less than 100% of the aggregate current index value; and that the issuer will promptly pay the member sufficient funds to purchase the warrant sold short in the event of a buy-in.