

margined separately; (3) provide for a Market Maker exclusion for proprietary trades of a "Security Futures Dealer" ("SFD") and allow for "good faith" margin treatment for the accounts of approved options specialists, market makers, and other specialists; (4) provide definitions relative to security futures contracts for application of this rule; (5) provide that security futures contracts transacted in a futures account shall not be subject to any provisions of NASD Rule 2520; (6) provide for money market mutual funds as defined in rule 2a-7⁵ under the Investment Company Act of 1940 (the "ICA"),⁶ to be used to satisfy margin requirements for security futures contracts provided certain conditions are met; (7) require that security futures contracts transacted in a securities account be subject to all other provisions of NASD rule 2520, particularly Rule 2520(f)(8)(B) ("Day Trading"); and (8) permit members for which NASD is the Designated Examining Authority ("DEA") to participate in the trading of security futures contracts.

In addition, NASD is proposing non-substantive technical changes to NASD Rule 2520.⁷

Below is the text of the proposed rule change. Proposed new language is *italicized*; proposed deletions are in brackets.

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2520. Margin Requirements

(a) Definitions

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

(1) The term "basket" shall mean a group of stocks that NASD 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, *except*

for security futures contracts (see paragraph (f)(11)(C)(ii)). 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 organization 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 organization 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 organization pursuant to section (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 an 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. *Any variation settlement received or paid on a security futures contract shall be considered a credit or debit to the account for purposes of equity.*

(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, or rules 400 through 406 under the Act or rules 41.42 through 41.48 under the Commodity Exchange Act ("CEA"); or

(2) the amount specified in section (c)[(3)] of this rule; or

(3) such greater amount as NASD [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). The minimum equity requirement for a "pattern day trader" is \$25,000 pursuant to paragraph (f)(8)(B)(iv)a. of this rule.

Withdrawals of cash or securities may be made from any account which has a debit balance, "short" position or commitments, provided it is in compliance with regulation T and rules 400 through 406 under the Act and rules 41.42 through 41.48 under the CEA, and after such withdrawal the equity in the account is at least the greater of \$2,000 (\$25,000 in the case of a "pattern day trader") or an amount sufficient to meet the maintenance margin requirements of this rule.

(c) Maintenance Margin

The margin that must be maintained in all 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, *except for security futures contracts*, "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.

(5) *The minimum maintenance margin levels for security futures contracts, long and short, shall be 20 percent of the current market value of such contract. (See paragraph (f) of this rule for other provisions pertaining to security futures contracts.)*

(d) No Change.

⁵ 17 CFR 270.2a-7.

⁶ 15 U.S.C. 80a *et seq.*

⁷ See NASD Rule 2520(b)(2); (b)(3); (e)(7)(B); and (e)(8). Telephone conversation between Patricia Albrecht, Assistant General Counsel, NASD, and Lisa N. Jones, Attorney, Division of Market Regulation, Commission, dated March 18, 2003.